

F623

JOINT APPENDIX

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 19,209

NORTH CENTRAL AIRLINES, INC.,

Petitioner,

v.

CIVIL AERONAUTICS BOARD,

Respondent.

On Petition for Review of Order
of the Civil Aeronautics Board

United States Court of Appeals
for the District of Columbia Circuit

FILED OCT 4 1965

Nathan J. Paulson
CLERK

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JOINT APPENDIX

[Filed April 6, 1965]

**IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT**

NORTH CENTRAL AIRLINES, INC.,	:	x
Petitioner,	:	
v.	:	No. 19, 209
CIVIL AERONAUTICS BOARD,	:	
Respondent.	:	

PREHEARING CONFERENCE STIPULATION

Pursuant to Rule 38(k) of the Court, and subject to its approval, the parties hereby stipulate and agree as follows with respect to the issues and the procedures and filing date for the joint appendix herein.

I

Issues

Petitioner is a local-service air carrier receiving subsidy mail pay pursuant to section 406(b)(3) of the Federal Aviation Act, 49 U.S.C. 1376(b)(3). The controversy here relates to its subsidy pay for the calendar year 1962, which is governed by the provisions of the so-called "Local Service Subsidy Class Rate I", a subsidy rate formula applicable to all local-service carriers which was made final as to petitioner by

Order E-16485, 34 C.A.B. 416, 418 (March 7, 1961). That rate order provided inter alia for a system of "profit-sharing", whereby each carrier would refund to the Board a portion of its after-tax profits each year in excess of a specified rate of return. The order described in detail how much after-tax profits were to be computed.

After scrutinizing the carrier's reports, and after informal conferences and correspondence, the Board in Order E-21163 (January 11, 1965) determined petitioner's profit-sharing refund for 1962 to be \$556,103, the balance of which sum the Board deducted on February 10, 1965 from petitioner's current subsidy for January 1965. The present petition for review challenges the Board's 1962 profit-sharing determination only with respect to a \$25,660 item included therein as the result of the Board's treatment of petitioner's federal investment tax credit for 1962.

The issues are:

1. Whether jurisdiction to review the actions of the Board here complained of lies in this Court under section 1006 of the Federal Aviation Act, 49 U.S.C. 1486, or section 10 of the Administrative Procedure Act, 5 U.S.C. 1009; or whether such jurisdiction lies only in the Court of Claims under the doctrine of Mohawk Airlines v. Civil Aeronautics Board, 329 F. 2d 894 (1964)?

2. If the Court has jurisdiction of the subject matter, whether petitioner is precluded from challenging the Board's determination by its failure to object before the Board to the terms of Order E-16485, supra, its failure to seek review of that order, and/or its acceptance of benefits thereunder?

3. If the Court reaches the merits, whether the Board's treatment of petitioner's investment tax credit for profit-sharing purposes is contrary to the provisions of section 38 of the Internal Revenue Code of 1954, in conjunction with section 203(e) of the Revenue Act of 1964; or is inconsistent with the provisions of the Class Rate order, Order

E-16485, governing petitioner's subsidy for the period in question; or is arbitrary, capricious, or otherwise unlawful?

The parties reserve the right in their respective briefs to rephrase the issues as above stated, without change of substance. Petitioner agrees that any grounds for reversal not urged in its opening brief shall be treated as abandoned for purposes of review herein, but reserves the right to respond on reply brief to any matters raised in respondent's brief.

II

Procedures with Respect to Printing of the Joint Appendix, and Use of Unprinted Portions of the Record

The joint appendix shall contain the materials required to be printed by the Rules of the Court, the materials designated by the parties as hereinafter provided, this stipulation, and the order of the Court approving the stipulation. At the time each party serves its brief, it shall also serve its designation of the portions of the certified transcript of record to be reproduced in the joint appendix. As soon as all such designations have been made, the petitioner, subject to Rule 16(a), shall cause the joint appendix to be printed, and shall file it within 10 days after the due date for the reply brief. Board counsel may release the certified transcript of record to any printer in the District of Columbia selected by petitioner to print the joint appendix.

All briefs shall cite the record by referring to page numbers in the certified transcript of record, in the form "(Tr. ____)." In the joint appendix, the record page number shall appear at the place where the material from each new record page begins, and a running head showing the record page with which each left-hand joint appendix page begins, or right-hand joint appendix page ends, shall appear at the outer top corner of such page. (The usual consecutive numbering of joint appendix pages shall appear at the top center of each such page.)

Any party, in brief or on oral argument, may refer to and rely upon any portion of the original transcript of record herein which has not been reproduced, to the extent that such portion may be material to the stipulated issues. Any such portions of the record thus referred to will be reproduced in a supplemental joint appendix if the Court so requires.

/s/ Raymond J. Rasenberger
Attorney for Petitioner

/s/ O. D. Ozment
Attorney for Respondent

April 6, 1965

[Filed April 8, 1965]

Before: Washington, Circuit Judge, in Chambers.

ORDER

Counsel for the parties in the above-entitled case having submitted their stipulation pursuant to Rule 38(k) of the General Rules of this Court, and the stipulation having been considered, the stipulation is approved, and it is

ORDERED that the stipulation shall control further proceedings in this case unless modified by further order of this court, and that the stipulation and this order shall be printed in the joint appendix herein.

Dated: April 8, 1965

[1]

ORDER NO. E-16173

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D. C.
on the 23rd of December, 1960

In the Matter of the

LOCAL SERVICE CLASS SUBSIDY : Docket 12004
RATE INVESTIGATION :

ORDER INSTITUTING PROCEEDING

By this order the Board is instituting a proceeding under Section 406 directed to the establishment of a uniform class subsidy mail rate for local service carriers effective January 1, 1961. This order will also reopen as of January 1, 1961 all final subsidy mail rates in effect for local service carriers on that date. The issue in this proceeding shall be limited to the question of establishing a class rate for the local service carriers.

For some time the Board and its staff have been studying the question of replacing the present system of determining subsidy mail rates for local service carriers on an individual carrier-by-carrier basis with a uniform rate formula which would be applicable to the local service carriers as a class. The Board believes that a class rate, if practicable, would have many advantages over the present system. Such a rate would enable the Board to eliminate lengthy open rate periods along with retroactive rate making, thus affording each carrier advance knowledge of the amount of subsidy support to be received for particular operations. Moreover, by requiring each carrier to operate

under a rate determined on the basis of the results of all members of the class, a class rate would create stronger incentives for greater operating efficiency, cost controls, optimum fare levels and economic scheduling than have hitherto existed under individually determined "cost-plus" rates.^{1/}

The Board now has under consideration a proposed rate formula under which a carrier's subsidy would be determined on the basis of its density of operations. The Board expects to complete its studies of this formula within a short period and anticipates that it will issue a Statement of Provisional Findings and Conclusions together with an Order to Show Cause proposing the establishment of a class rate along the lines of the formula now under consideration. In the meantime, the Board believes it desirable to institute this proceeding reopening all local service final subsidy rates effective January 1, 1961 so as to enable the Board to establish the class rate effective on the first of the year.

^{1/} In practice, individual rates are based on the difference between operating revenues and operating expenses, plus a fair return minus disallowances in accordance with established rate policies.

There are at the present time final local service subsidy rates in effect for six of the thirteen local service carriers. This order will reopen each of these rates as of January 1, 1961 to the limited extent set forth below. Thus, the issues in this proceeding shall be confined solely to the matter of establishing a class rate for the local service carriers. To the extent that a class rate may not be established as of January 1, 1961 for any carrier whose final rate was reopened by this order on January 1, 1961, such final rate will continue as the final mail rate on and after January 1, 1961. Any carrier is, of course, free, during the pendency of this proceeding, to file a petition reopening its

rate as to all issues, but such petition shall, of course, relate only to the period on and after the date of such filing. Similarly, the Board may, pending these proceedings, reopen the rate of any one or more carriers as to all issues, on a prospective basis.

ACCORDINGLY, IT IS ORDERED THAT:

1. Proceedings are hereby instituted for the sole purpose of determining whether the Board should establish, effective January 1, 1961, or such later date as the Board shall determine to be proper, a class rate based upon a single rate formula or scale of rates for the carriers named in paragraph 3, under Section 406 of the Federal Aviation Act, and to fix and determine such rates.^{2/}

2. Each final mail rate established under section 406 for any carrier named in paragraph 3 in effect on January 1, 1961 be and it hereby is reopened as of January 1, 1961 solely for the purpose set forth in paragraph "1" above.^{3/}

3. Allegheny Airlines, Inc., Bonanza Air Lines, Inc., Central Airlines, Inc., Frontier Airlines, Inc., Lake Central Airlines, Inc., Mohawk Airlines, Inc., North Central Airlines, Inc., Ozark Air Lines, Inc., Pacific Air Lines, Inc., Piedmont Airlines, Southern Airways, Inc., Trans Texas Airways, Inc., and West Coast Airlines, Inc., are hereby made parties to this proceeding.

4. The issue involved herein shall be limited to that set forth in paragraph 1; provided, however, that, in accordance with Rule 303 of the Rules of Practice, any carrier may file a petition stating that its rate is,

^{2/} This order is not intended to disturb the service mail rates established under Section 406(c).

^{3/} At the present time the following final orders under Section 406 are in effect: Bonanza Air Lines, Inc., E-15808, September 22, 1960. Central Airlines, Inc., E-15753, September 8, 1960.

3/ Cont'd.

Lake Central Airlines, Inc., E-15903, adopted October 11, 1960 and effective October 17, 1960.

Ozark Air Lines, Inc., E-16085, November 30, 1960.

Piedmont Aviation, Inc., E-15967, October 28, 1960.

West Coast Airlines, Inc., E-15730, September 2, 1960.

In addition, the Board has issued a show cause order proposing a final rate for Pacific Air Lines, Inc., E-16129, December 9, 1960. Any final order in this latter case will be subject to this reopening order.

[3]

or is likely to become, inadequate, and setting forth the reasons therefor together with supporting documents, in which case the carrier's rate shall be considered open as to all issues. Such petition shall have the effect of reopening such rate as of the date when filed.^{4/} Any issue other than the issue of the establishment of class rates shall be dealt with in separate proceedings.

5. This order shall be served upon all parties to this proceeding and the Postmaster General.

By the Civil Aeronautics Board:

/s/ Robert C. Lester
Secretary

(SEAL)

4/ Nothing herein is to be construed to prevent the Board from reopening any carrier's rate as to all issues effective on the date of the order reopening such rate.

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E-16380

Adopted: February 16, 1961

**STATEMENT OF PROVISIONAL FINDINGS AND CONCLUSIONS
BY THE BOARD:**

This proceeding was instituted by Order E-16173, December 23, 1960, for the purpose of determining whether the Board should establish

a class rate for local service carriers effective January 1, 1961. By this statement and the attached Order to Show Cause we are directing the thirteen local service carriers to show cause why the Board should not establish a class rate for the local service industry.

The proposed class rate consists of a scale of rates based upon volume of operations per station: as revenue plane miles per station increase, the unit subsidy rate per available seat mile flown is reduced.^{1/} The monthly

^{1/} Throughout this statement, available seat miles refers to seat miles computed on the basis of a standard number of seats for the respective aircraft types as follows:

DC-3	24 seats
F-27, M202, CV240	40 seats
CV340, CV440, M404	44 seats
CV540	52 seats

subsidy payable to each carrier under the class rate will be based upon (1) the carrier's available seat miles during the month times (2) a rate per seat mile varying with the revenue plane miles per station per day for the particular carrier in the given month in accordance with the scale of rates contained in Appendix I. No additional subsidy is paid for operations in excess of the 600 plane miles per station per day. The proposed class rate also contains a profit-sharing formula under which the carriers will refund to the Board (1) 50 percent of profits between a fair rate of return and a return of 15 percent on investment, and (2) 75 percent of profits in excess of a return of 15 percent on investment. Earnings deficiencies will be permitted to be carried forward to two future years as an offset against any future excess earnings.

I. GENERAL

The matter of a class rate for local service carriers has been under active consideration by the Board and its staff for approximately three years. On January 24, 1958, we announced that we had

"...instructed our staff to consider . . . whether any revision of the existing standards is required in the light of the present state of development of the local service carrier industry. With no intent to circumscribe the study in any way, the staff has been advised that we have a particular interest in a system providing effective subsidy control through a well designed incentive device² which would require a minimum of regulatory intervention."

Subsequently our staff, working with the local service industry, developed various plans for determination of subsidy by class rather than by individual

2/ Mohawk Airlines, Mail Rates, Docket 7277, Order E-12139,
January 24, 1958, p. 5.

carrier basis. In January 1960, the Board after studying the progress thus far concluded that none of the plans which had been developed to that date was satisfactory and directed its staff to give first priority to the fixing of rates for the local service carriers on an individual basis. At the same time, unwilling to abandon the concept of a class rate, the Board directed the staff to continue to work on the project. The efforts of the staff, working with the industry, have produced a class rate plan which appears to meet the essential requirements for a workable class rate.

The proposed class rate represents a radical departure from the methods ordinarily used by the Board to fix subsidy rates. Hitherto the Board has typically determined rates for each carrier either for a past period or for a prospective future period on the basis of an analysis of the particular carrier's own operating results and forecasts.

The proposed class rate, while constructed on the basis of each individual carrier's need, is nevertheless a rate which is stated in terms of a class of carriers. While the amounts payable to any given carrier will vary in accordance with the rate formula depending upon volume of service, equipment utilized and density of operations, the same formula will be applicable to all carriers in the group. As detailed below, the Board believes that the adoption of a class rate will provide stronger incentives for economical carrier operations than those which prevail under the system of individual rates and that it will result in general in a long term reduction in subsidy costs and a healthier and more vigorous local service industry.

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II. PRESENT SYSTEM OF SUBSIDY DETERMINATION

With one exception,^{3/} the Board has always established subsidy rates on an individual carrier basis. Two types of subsidy rates have been employed: (1) a past period rate which is determined on the basis of actual results, and (2) a future rate which is based upon forecast operations. In either case, however, the same basic approach has been followed. The financial and traffic reports and forecasts are subjected to audit and analysis, and adjustments are made to reflect more accurately the earnings of the period as well as to disallow expenses and investment found to be uneconomical or inefficient or not in accordance with statutory standards. After all adjustments, a carrier's subsidy rate is fixed in an amount sufficient to meet its own break-even need (the difference between expense and other revenues) plus a reasonable return on investment after taxes.

The present method of individualized subsidy determination is not without its advantages. It permits the fixing of rates which are tailored to each carrier's specialized requirements and it provides a relatively precise method of controlling the level of earnings of each carrier. On the other hand, the system has a number of deficiencies.

As applied to local service carriers (1) it has resulted in extended open rate periods, (2) it fails to afford management flexibility for maximum initiative and incentive for maximum efficiency and economy and (3) it necessitates a substantial amount of regulatory involvement in managerial questions.

3/ American Airlines, Inc., et al., Mail Rates, 14 C.A.B. 558 (1951).

1. The open rate problem. Generally speaking, where an existing final future subsidy rate becomes inadequate or excessive, the rate is reopened under section 406(a), either on petition of the carrier or by order of the Board. Typically, a rate is reopened because the addition of new routes or transition to larger equipment serves to render the existing rate inadequate. Frequently it is necessary to obtain operating experience with the new route before a final rate may be fixed for the new operation. This fact, plus the pressure of workload, results in carriers' rates remaining open for longer periods than are desirable. Where carriers' rates are open for long periods, it is necessary to fix the rate for the past operation on a retroactive basis.

Although the goal of the Board is to have carriers on final future rates, the past history indicates the difficulty of achieving that goal. For example, during the period 1958-1960, the local service carriers were on an open rate status over 80 percent of the time. The problem is illustrated by the calendar year 1960 in which the Board instituted a top priority program to finalize the rates for the eleven local service carriers' rates which were open at the beginning of the year. As of the end of the year, the Board was able to close seven of the eleven cases, leaving four remaining to be completed. However, four final rates were reopened during 1960 and January 1961, by carrier petition. Thus, despite a year of intense rate activity, eight of the thirteen local

service carriers are currently on an open rate status. So long as the present system of subsidy determination is retained, it does not appear likely that open rate periods can be avoided for sufficiently sustained periods of time for a substantial segment of the local industry.

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The pendency of long open rate periods is undesirable from the standpoint of both the carrier and the government. As long as a carrier's rate is open, neither the carrier nor the government can know what the final subsidy for the period will be. The earnings which the carrier reports to the public, to stockholders and to lending institutions are necessarily subject to adjustments either upward or downward. As a result, the earnings statement becomes an unreliable basis upon which financial commitments can be predicated. Financing is difficult under such circumstances and the carriers' general credit position is adversely affected. Moreover, during open rate periods the Board has been compelled to follow a temporary rate policy which provides the government with a reasonable cushion in the event that reported expenses are disallowed, in order to avoid recapture of excess subsidy. The result is that while on a temporary rate the carrier normally cannot show net earnings. Open rate periods also create substantial burdens on the Board and its staff since the process of screening past results is time-consuming and work must frequently stop to process temporary rate petitions which are often filed by carriers in urgent need of additional temporary subsidy payments to support their required operations. Finally, the pendency of open rate periods aggravates the incentive problems which are present in any system of individually determined subsidy rates. These problems are discussed immediately below.

2. Incentives. Expenses and capital costs incurred under honest, economical and efficient management and in accordance with the statutory developmental standard are required by section 406 to be

underwritten with subsidy. A carrier thus has less incentive to maximize efficiency while on an open rate

than on a final rate basis. Carriers are aware that additional schedules will be underwritten with subsidy, provided they meet generalized standards formulated by the Board, but they lack maximum incentive while on an open rate to schedule their operations with maximum efficiency. When a carrier is on a final, individually determined subsidy rate, strong incentives to economical operations are present, but such rates may be reopened by the filing of a petition or by Board order. The ability to reopen tends to weaken the pressure to live within the final rate. It is also apparent that the spark which competition normally provides to American business enterprises is missing under a system of individual retroactive subsidy determinations.

3. Board Involvement in Managerial Questions. The absence of normal business incentives under a system of individual carrier subsidy rates necessitates a detailed and thorough scrutiny by the Board of all areas of a carrier's operations in order to determine whether the carrier meets the statutory standards of honest, economical and efficient management as well as whether the operations serve a developmental purpose. To the extent that the Board determines that the carrier has not met these standards, disallowances of expenses and investments are made in proper amounts. The task of evaluating a carrier's performance is at best a complex and difficult one. Whether, for example, a carrier should have added a particular schedule, or whether its level of maintenance expense is excessive requires extensive analysis of costs and revenues, comparisons with other carriers, etc. Despite the development by the Board of standards and criteria for testing carrier efficiency, the process necessarily involves a substantial degree of judgment and subjectivity and adds an additional

element of uncertainty in the operation of the carriers.

4. Summary. In summary, the present subsidy system as applied to local service carriers does not provide the best framework for the continued development of the dynamic and growing local service industry. It has imposed unnecessary administrative burdens on the Board, and has failed to create the best or strongest incentives to managerial efficiency. Finally, the present system has not enabled the carriers by and large to achieve reasonable earnings. Reference to any recent tabulation of reported earnings of the thirteen local service carriers reveals losses reported by a number of carriers, and completely inadequate earnings reported for the group. The reported earnings deficiency is to some extent misleading, since to a considerable degree the deficiency is eliminated when a retroactive rate is established. It is clear that when measured against the standards of a fair return which we have used in the past of 7 percent for past periods and between 8 percent and 12.75 percent for future periods, the results of the individual carriers as well as the carriers as a group have fallen far short of the earnings necessary to maintain financial integrity and it is clear that unless improvement in the earnings is forthcoming the carriers will find it increasingly difficult to attract needed capital. While part of the carriers' poor showing in the past may be attributable to factors over which carrier managements have had control, we are nevertheless convinced that a substantial part of the problem is traceable to the employment of the carrier-by-carrier approach to subsidy determination and the sustained periods of open rates subject to retroactive adjustment.

Finally, it must be noted that whereas the carriers' earnings have been below par, the subsidy bill has been increasing in terms of total dollars as well as recently in terms of the unit of service, as shown in

Appendix J.

To a substantial extent the increased subsidy is directly related to the additional routes which the Board has awarded to the local service carriers. Nevertheless, the Board is of the opinion that a soundly conceived system of subsidy payment which creates strong incentives to managerial efficiency and avoids the weaknesses inherent in the carrier-by-carrier approach has a good chance of effecting a reversal in the upward subsidy trend.

III. ADVANTAGES OF A CLASS RATE

The Board believes that a class rate would have many advantages over the present system of individual carrier-by-carrier rate-making.

1. Incentives of a Class Rate. As we pointed out in our order instituting this proceeding, by requiring each carrier to operate under a rate determined on the basis of the results of all members of the class, such a rate would create stronger incentives for greater operating efficiency, cost controls, optimum fare levels and economic scheduling than have hitherto existed under individually determined rates.

As the Supreme Court stated, "The uniform rate for the class is an important regulatory device" since it "... forces carriers within a given class to compete in securing revenue and reducing and controlling costs.^{5/}" By eliminating the

^{5/} Transcontinental & Western Air v. C.A.B., 336 U.S. 601, 606-607 (1949).

carrier would be forced to live within a rate determined on the basis of industry results rather than its own particular performance. The cost levels of any particular carrier will have only a token effect on the level of the class rate. Accordingly, carriers should generally tend to be more cost conscious than they have been in the past.

Moreover, local service carriers have lacked maximum incentive in the past to charge optimum passenger fares. Since subsidy has generally been available to make up the difference between revenues and expenses, a carrier contemplating fare increases is faced with the prospect that such increases will be used by the Board to reduce subsidy. Since the level of a class rate will not be directly affected by any particular carrier's fare adjustments, each carrier would retain to a substantial degree the benefits of fare increases and would be encouraged to seek higher fares, where it is believed that such fares would not have an adverse effect upon traffic and would improve profit.

2. Elimination of extended open rate periods. The second advantage of the class rate would be the elimination of extended open rate periods. Under a class rate, each carrier would have advance knowledge of the final subsidy support to which it would be entitled for a given scale of operations, and would therefore be enabled to budget its operations accordingly. Thus, the uncertainties of the present system will be eliminated. Moreover, the elimination

of extended open rate periods will result in more meaningful carrier financial statements, in that subsidy received will not be subject to retroactive readjustment by the Board, except to the limited extent of the profit-sharing plan. The avoidance of open rates should go far towards enabling carriers to finance their operation on a businesslike basis.

3. More effective control of subsidy. Under a system of individual carrier subsidy determinations where lengthy open rate periods exist, the problem of control of the level of subsidized operations is rendered difficult because the carriers themselves are not under maximum pressure to operate with economical scheduling practices. In other words, a carrier has an incentive under the present system to maximize the scale of its operations to the extent that it believes that the Board would underwrite them. Thus, subsidy control becomes to some extent a negative function of the Board. Under a soundly conceived class rate, subsidy control can be effected by the incentives built into the formula. Thus, under a class rate, subsidy control can well be in each individual carrier's own self-interest from a profit motive standpoint.

4. Operating flexibility. Under a class rate each carrier will "sink or swim" with the subsidy provided by the industry-wide formula. Management will have greater flexibility in tailoring operations subject to the general regulatory provisions of the Act other than section 406. The carrier will reap the benefit of successful use of that flexibility but will pay the penalty in the form of inadequate earnings for improper use of flexibility. The use of the plane miles per station factor produces a declining rate per available seat mile

as schedules are increased, thus creating a strong pressure on the carrier to increase schedules only when justified by reasonable load factors, and conversely, to reduce schedules which are not required in terms of reasonable loads.

IV. LEGAL BASIS FOR ESTABLISHMENT OF CLASS RATE

The Board is of the opinion that it has the requisite legal power to establish class subsidy rates. Section 406(b) specifically provides that the Board may "fix different rates for different air carriers or

classes of air carriers, and different classes of service". This authority is stated in general terms broad enough to include both subsidy mail rates as well as service compensation. There appears to be nothing in the legislative history of the Act to indicate that Congress intended the class rate provision to be applicable only to service rates.

It is, of course, true that the "need" provision of section 406(b), which is the source of our authority to provide subsidy, speaks in terms of "the need of each such air carrier for compensation" sufficient to enable it to maintain and continue the development of air transportation. But there is no inconsistency between the concept of a class rate and the concept of individual carrier need. A rate can be fixed for a class of carriers and still provide each individual carrier with an opportunity to earn an amount equal to its own individual "need" under the statute. Thus, whether the Board can fix a class rate depends entirely upon the homogeneity of the class and the extent to which essential differences in the inherent characteristics of a carrier's routes are

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taken into consideration in constructing a class rate.

Indeed, this is not the first occasion that the Board has established a class mail rate containing subsidy. In the Big Four Mail Rate Case^{6/}, the Board established a rate of 63 cents per mail ton mile for the Big Four carriers for the period 1947-50. Although stated in terms of a rate per ton mile, the rate in fact contained a substantial amount of subsidy. The Board justified the establishment of the class rate on the ground that "the Big Four constitute a homogeneous group for rate-making purposes, and . . . had a comparable opportunity, under conditions of economical and efficient management, to earn a fair profit under a uniform mail rate."^{7/}

Support for the Board's power to establish a class subsidy rate is found in the Supreme Court's decision in the TWA case.^{8/} In that case, the Court held that the Board did not have the power to fix mail

rates for a period prior to the date of institution of a mail rate proceeding. The Court asserted that a contrary construction "would not harmonize with the apparent design of the Act" since

" . . . §406(b) authorizes the Board to fix rates for 'classes of air carriers.' It is plain that the uniform rate for the class is an important regulatory device. For §2(d) of the Act looks to the sound development of an air transportation system through competition. A uniform rate forces carriers within a given class to compete in securing revenue and in reducing or controlling costs. If the Board had authority on the basis of the carrier's needs to make rates retroactive to any point of time, there would be a powerful incentive to seek relief from the uniform rate, not to live within it." (Footnotes omitted.)⁹

^{6/} American Airlines, et al., Mail Rates, 14 C.A.B. 558 (1951).

^{7/} Ibid. at page 566.

^{8/} Transcontinental & Western Air v. C.A.B., 336 U.S. 601 (1949).

^{9/} Ibid. at pp. 606-7.

We do not overlook such cases as Delta Air Lines v. Summerfield.^{10/} None of these cases involved class rates. They stand for the proposition that the Board cannot ignore amounts affecting a carrier's need on grounds of economic "policy." However, the Board does not propose to ignore carrier need on the basis of policy or other grounds. On the contrary, the class rates proposed herein are determined on the basis of individual carrier needs and in our opinion should provide earnings consistent with each carrier's need under honest, economical and efficient management.

Of course, under any class rate, some members of the class will be less favorably or more favorably situated than others. The returns,

as well as the amounts of subsidy payable, to a carrier under a class rate will not be identical with those which might otherwise be paid under an individual carrier-by-carrier approach. This is inherent in a class rate.

V. HOMOGENEITY OF THE LOCAL SERVICE GROUP

A number of characteristics having a direct relationship to the economy of air carrier operations are common to the local service carriers and support their treatment as a class for rate-making purposes.

The operating authorities held by these carriers represent the basic common characteristic and are the cause of the subsidy support necessary for these carriers. These operating authorities have two principal features: first, they authorize service to and from the smaller cities, and service between the smaller cities and larger traffic centers; Second, to assure the maintenance of service required by the smaller communities, the operating authorities held

^{10/} 347 U.S. 74 (1954). See also Western Air Lines v. C.A.B., 347 U.S. 67 (1954), and American Overseas Airlines v. C.A.B., 254 F. 2d 744 (D. C. Cir. 1958).

by local service carriers restrict the operation of nonstop services by specific conditions spelled out in the carriers' certificates. These restrictions require provision of stated volumes of service to the intermediate cities on a particular route before nonstop services may be operated. Except in isolated instances, these conditions effectively preclude competition between local service and trunk carriers as respects the larger pairs of points.

The effects of the foregoing, in terms of the economics of air carrier operations, are immediately evident in the important characteristic of traffic volume. In the twelve months ended June 30, 1960, the

largest and the smallest local service carriers experienced traffic volumes of 6.4% and 1.2%, respectively, of the average trunk carrier, with the average local service carrier experiencing 3.2% of the average trunk carrier's volume. Traffic densities, experienced in numbers of revenue passengers per route mile per day, ranged from 35.5 to 210.9 during this period. By contrast, trunk carrier densities ranged from 509.5 to 2,421.3 per day.

The frequencies required to serve these traffic volumes necessarily fall within a relatively limited range. During the twelve months ended June 1960, eight of the thirteen carriers experienced a daily route mile turnover of approximately 5 to 8 daily with five reporting daily frequencies of 10 to 12.6. By comparison, trunk frequencies ranged upward to 51.4.

The equipment employed in operation of the routes here involved is limited to twin-engine types and no equipment exceeds 52-passenger capacity. The average capacity afforded in fiscal 1960 actually did not exceed 40 available seats per mile for any carrier.

Because of the nature of the routes operated, the average stage length (length of hop) and average length of passenger journey experienced by local service carriers were similarly low. No carrier in the group approached the figures experienced by the smallest trunk carrier so far as these two indices are concerned.

Other comparisons of significant operating data are found in Appendix K.

VI. CONSTRUCTION OF THE CLASS RATE

As previously indicated, the class rate consists of two principal parts: (1) a scale of rates per available seat mile which varies inversely with revenue plane miles per station, and (2) a profit-sharing formula.

1. Rate Scale. The proposed class rate is based upon an observed correlation between density of operations and need. There is no question that local service carriers' needs per available seat mile operated vary inversely with the density of operations. This is true in greater or less degree depending upon the particular measure of density used. The Board's studies indicate that definite correlations exist between need and such factors as revenue plane (or seat) miles per unduplicated route mile, departures per station, revenue ton miles per station, etc. The question as to which of these factors should be used as the basis for the class rate is a matter of judgment. In selecting the density factor to be used as the basis for the class rate, we have considered not only the degree of correlation to need produced by the various factors, but also the effect on managerial incentives which can be expected from the use of alternative density factors. The factor of revenue plane miles per station per day appears to satisfy both of these considerations.

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The scale of rates was determined on the basis of the results for the year ended June 30, 1960, as a base period. Each carrier's need per available seat mile was computed on the basis of the base period results, as adjusted. After adjustments, the computed need represents the forecast seat-mile subsidy requirement for each carrier for the year commencing January 1, 1961. Need was determined as follows:

a. Breakeven need. Reported expenses for the base period were adjusted (1) in order to arrive at actual base year costs, by means of accounting adjustments for out-of-period items, standardization of depreciation and other accounting adjustments designed to reflect the actual operating results for each carrier for the period; and (2) to disallow certain types of expenses which are not recognized for mail rate purposes. These disallowances include such items as executive salaries in excess of \$25,000, entertainment expenses, charitable contributions,

lobbying expenses, etc. The adjustments for each carrier are set forth in Appendix E.

In constructing the breakeven need for each carrier, we have not made the usual disallowances for excess schedules or for excessive cost levels. The formula contains its own penalties for the operation of excess schedules: generally speaking, the operation of additional revenue plane miles over the carrier's system will produce less subsidy per seat mile. Moreover, since the rate is a rate per seat mile operated and since the operation of excess schedules does not increase the unit rate per seat mile, our decision not to adjust for excess schedules in fixing the class rate does not increase the level of the class rate.

The Board has made an analysis of its determination in recent local service mail rate cases with respect to excess cost levels. By and large the disallowances have been relatively minor in amount. Moreover, the industry results include not only the high costs of some carriers, but also below-average costs of others. It is the Board's judgment that, under all of the circumstances, the inclusion of both extremes of cost in the class rate formulation will produce a reasonable end result consistent with the need of each carrier under the statutory standard of "honest", economical and efficient management."

In this connection, we have considered whether we should provide an allowance for inflation over and above the operating expenses incurred during the fiscal year, 1960. There is no doubt that for the past several years expenses per available seat mile have shown a steadily rising trend for the carriers as a group. We have determined, however, to make no specific allowance for this factor in this initial class rate. Our determination is based essentially on three considerations.

First, a substantial amount of the increase in seat mile costs is clearly associated with the integration of more modern equipment. As personnel become experienced with the new aircraft types and as mechan-

ical and operational problems are solved, unit costs will tend to decrease. For the majority of carriers, the year 1961 should begin to see a turning point in the cost bulge associated with the integration of new equipment. A second consideration is the fact that the establishment of class rates should act as a powerful incentive

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to control costs. Indeed, this incentive aspect is one of the most important reasons for the establishment of a class rate. Finally, the flexibility inherent in the proposed formula, under which a carrier will be free to adjust its schedules on a system-wide basis in order to produce optimum earnings consistent with standards of adequate service, means that carriers will be enabled to make changes in their schedules if cost inflation dictates.

On the revenue side, we have made a further adjustment to reflect the passenger fare increase authorized by the Board for effectiveness July 1, 1960, and estimated to produce for each carrier an effective increase of 2 1/2 percent plus 90 cents per ticket.

b. Investment Base. In determining the adjusted need for each carrier, the investment base used was the investment as of June 30, 1960, for each carrier rather than an average investment for the year ended June 30, 1960. The rising trend in investment per available seat mile has been such that the use of the year-end balance sheet has understated rather than overstated the seat mile investment for the subsequent year. There is no reason to anticipate that this trend will not continue during 1961.

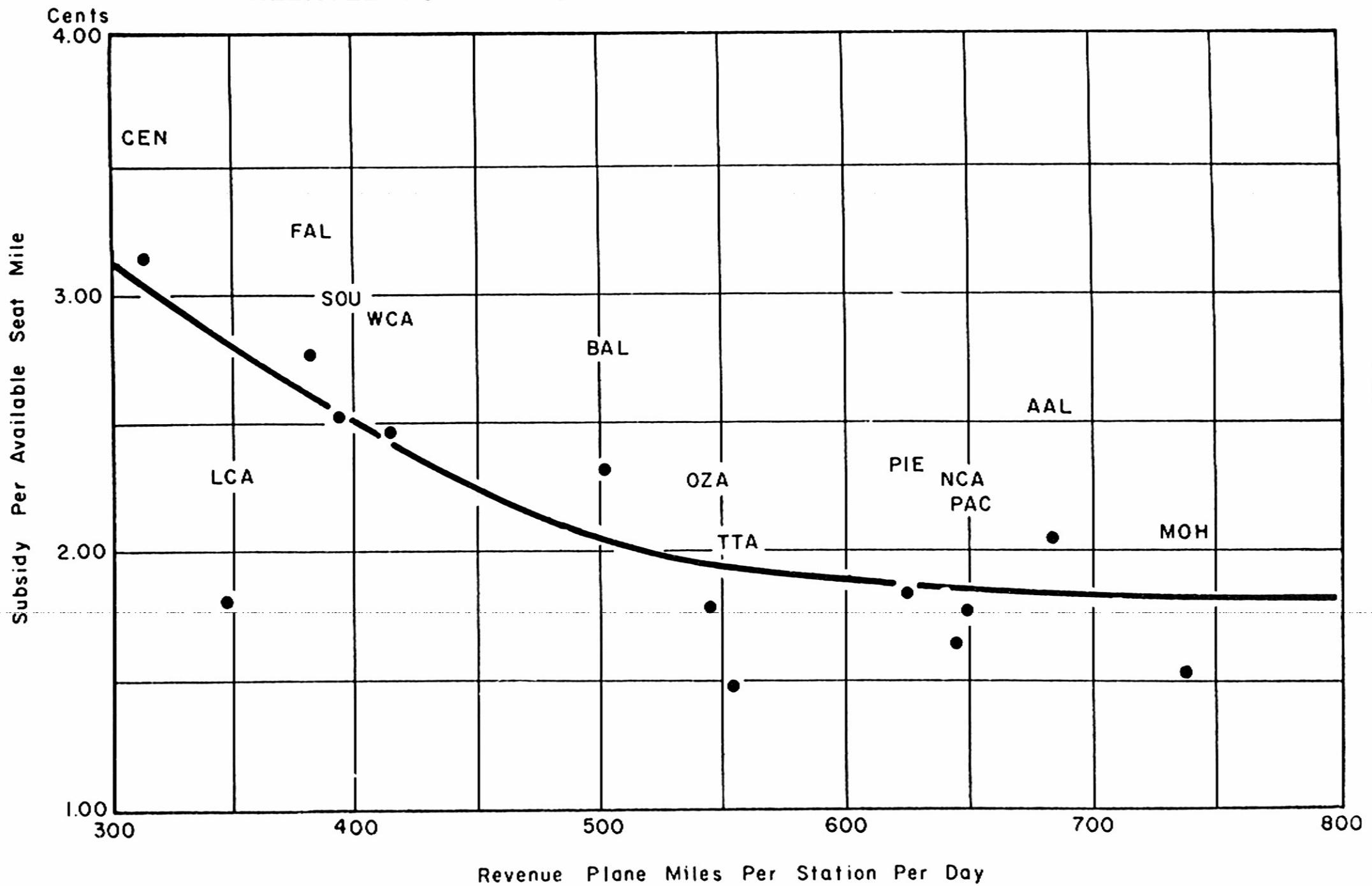
Consistent with the treatment of expenses, previously discussed, adjustments have been made to each carrier's investment. Among the more significant adjustments are (1) transfer of 75 percent of current notes payable from current liabilities to long-term debt, (2) elimination of unamortized debt discount and expense, (3) elimination of nonoperating property and equipment, (4) elimination of equipment deposits, (5) addition of estimated retroactive

subsidy not reflected in the balance sheet as reported, (6) reversal of accrued vacation reserves, and (7) depreciation adjustments to reflect the standard depreciation bases used by the Board.

c. Return. The return element has been calculated for each carrier based upon the Board's decision in the Local Service Rate of Return Investigation, Docket 8404, i.e., a return of 5.5% on debt and 21.35% on common stock equity applied to actual capital structure and subject to minimum and maximum over-all returns of 9% and 12.75%, as well as a floor of 3 cents per revenue plane mile flown. As computed, the weighted average return for the 13 carriers is 10.02%.

In reaching our decision to adhere to the formulae announced in Docket 8404, we have not overlooked contentions made on behalf of some carriers that the use of a profit element based upon the actual debt-equity capital structure of the industry would conflict with the principles announced in the Rate of Return Investigation. The argument is that the use of actual capital structures would tend to freeze industry debt structure at its present high level. In Docket 8404 we rejected the use of an over-all rate of return to be applied to each carrier irrespective of its own capital structure because we found that (a) if the return were based upon the industry average capital structure, it would tend to freeze the existing undesirable high debt structure, and (b) if the return were based upon a more desirable capital structure it would result in windfalls to most of the carriers. Accordingly, we determined to construct each carrier's return on the basis of its own capital structure thereby providing an incentive to each carrier to reduce the proportion of debt to equity in its capitalization. The necessity of establishing a return for class rate purposes thus raises in a different form the dilemma which we faced in Docket 8404, since by the very nature of a class rate each carrier cannot be provided with an individually tailored rate of return. On the other hand, since for profit-sharing purposes the amount of return which a carrier will be

SUBSIDY REQUIREMENT PER AVAILABLE SEAT MILE RELATED TO REVENUE PLANE MILES PER STATION PER DAY



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allowed to retain will depend in part upon its own capital structure, the carriers will continue to have an incentive to improve their capital structures. For this reason as well as in view of the inherent flexibility of the class rate and our desire to avoid the use of a return which at present industry capitalizations would provide a windfall to the industry as a whole, we will use the actual debt-equity structure for each carrier in constructing the class rate.

d. Taxes. The tax allowance is based upon the 52 percent Federal income tax rate applied to net income, calculated as above, less interest deduction.

e. Construction of Rate Scale. From the above analysis a need for each carrier was computed consisting of the sum of its breakeven need, return allowance and taxes. The total subsidy requirement for the thirteen local service carriers, based upon the mileage operated during the year ended June 30, 1960 was approximately \$53,300,000. The subsidy per available seat mile ^{10a/} was derived for each carrier by dividing the carrier's need by the number of available seat miles operated during the period. A chart was drawn on which each carrier's need per available seat mile was plotted against its density factor. This chart is reproduced on the opposite page. A plotting of the points indicated a clear correlation between revenue plane miles per station and need per available seat mile.

The rate scale was determined on the basis of a curve which was drawn by visual inspection of the data in such manner as to produce the smallest deviation

^{10a/} As indicated in the footnote on page 1, standard seats have been used. Although the CV-440 can physically accommodate as many as 52 seats, it appears necessary to use the same number of seats for CV-340 and CV-440 since they are essentially the same aircraft type. The expense of converting a CV-340 to a CV-440 is far less than the additional subsidy which would be payable to a carrier if the 440 standard seats were to be pegged at 52, the maximum now being used by one local service carrier. Thus, failure to standardize seats as between 340s and 440s would appear to pave the way for manipulations of a carrier's subsidy through conversion of aircraft for the intended purpose of increasing subsidy.

; between the curve and the individually plotted points and at the same time to produce a rate level which would result in computed subsidy of approximately \$54,000,000 for the volume of operations conducted by the carriers in the year ended June 30, 1960. This curve forms the basis of the rate formula. The curve was converted into a scale of seat mile rates.

f. Floor and Ceiling Rates. As indicated above, the formula provides a scale of rates which vary from 3.11 cents per available seat mile for a density factor of 300 revenue plane miles per station per day to a low of 1.90 cents per available seat mile for a density factor of 600 miles per station. In the event that the carrier's operations fall below 300 plane miles per station per day, its rate would be computed on the basis of a maximum seat mile rate of 3.11 cents times the actual number of available seat miles operated. During the base period no carrier's density was below 300, and the forecast operations indicate generally higher densities for the future.

The formula also contains a ceiling with respect to operations in excess of 600 revenue plane miles per day. In effect, no additional compensation will be provided for such operations. Carriers will be expected to so schedule their operations that mileage operated in excess of the ceiling density factor will be self-sufficient.

2. Profit-Sharing. The second part of the formula is the profit-sharing element. Although the Board is of the opinion that the class rate proposed here will meet each carrier's statutory "need" under honest, economical and efficient management, for the future period beginning January 1, 1961, it is apparent that any class rate is bound to produce a wider variation in individual

returns than would be the case under individually tailored rates.^{11/} This factor is underscored by the experimental and novel character of the proposed class rate. At this point, in the absence of experience under a class

rate it is difficult to predict with certainty the financial results for particular carriers since this will depend in large measure upon the carriers' scheduling practices, as well as the extent to which the various incentives built into the formula are effective in reducing carrier needs. In view of these uncertainties, the Board believes that it is appropriate to include in the class rate formula a profit-sharing plan under which a portion of earnings in excess of a prescribed rate of return would be repaid to the government. Under the proposed formula, carriers would be permitted to retain all earnings up to the rate of return calculated in accordance with the principles established by the Board in the Local Service Rate of Return Investigation, Docket 8404.^{12/} Under that decision, each carrier's return is determined by application of a rate of 5.5 percent on debt capital and 21.35 percent on common stock capital, based upon its own capital structure, with a floor of 9 percent and a ceiling of 12.75 percent, but in no event less than 3 cents per revenue plane mile flown. Although none of the local service carriers had outstanding preferred stock prior to January 1, 1961, we have made provision for the application of a rate of 7.5 percent to preferred stock. The 7.5 percent rate is based on the cost of the recently floated convertible preferred stock issue of Lake Central Airlines, Inc.

11/ Where an individual subsidy rate appears to result in subsidy in excess of the carrier's need, the Board ordinarily reopens the rate to restore the subsidy to a fair and reasonable level. However, the question of reopening a class rate is necessarily geared to the need of the carriers as a class, without reference to the profit position of an individual carrier.

12/ Order E-15696, August 26, 1960.

The earnings for purposes of profit-sharing will be computed on an annual basis. For this purpose earnings will be as set forth in the carrier's reports filed in accordance with the uniform system of accounts.

These reports will be subject to adjustment (1) to standardize depreciation in accordance with the service lives and residual values employed by the Board in fixing mail rates, (2) to make other accounting adjustments necessary in order to reflect the true earnings of the carrier, and (3) to disallow those expenses which are customarily not recognized for subsidy purposes including expenses in such categories as charitable contributions, executive salaries in excess of \$25,000, etc. These are set forth in detail in the rate provisions.

Revenues from non-transport activities such as fixed base operations and other activities unrelated to the certificated services will be included along with related investment in determining earnings for purposes of profit-sharing only where such activities reduce subsidy requirements. Any earnings deficiencies from such non-carrier activities will be borne by the carrier.

Capital gains will not be treated as part of earnings for profit-sharing purposes but will be treated in accordance with the provisions of Order E-14104, dated June 24, 1959, and Part 235 of the Board's Economic Regulations, promulgated in accordance with Section 406(d) of the Act. Thus, under these provisions, any capital gains which are not reinvested in accordance with the statute, the order and the regulations will be used in their entirety to reduce subsidy payable to the carrier, in the same manner as is done under individually fixed

rates. Capital gains reinvested in accordance with the terms of the statute and the regulations will continue to be retained by the carrier.

VII. REASONABLENESS OF CLASS RATE

Based upon tests of the class rate as applied to the individual carriers for the base period and considering the incentives built into the formula and its inherent flexibility, the Board finds that the proposed class rate is fair and reasonable and meets the statutory requirements

of the "need of each air carrier under honest, economical and efficient management" for compensation sufficient to maintain and develop air transportation as required.

Comparison of Class Rate Subsidy with Individual "Need"

12-months ended June 30, 1960

	<u>Class Rate Subsidy</u>			<u>Percent Deviation of Class Rate Subsidy from "Need"</u>	
	<u>Before Profit Sharing</u>	<u>After Profit Sharing</u>	<u>Individual "Need" 13/</u>	<u>Before Profit Sharing</u>	<u>After Profit Sharing</u>
	<u>(000)</u>	<u>(000)</u>	<u>(000)</u>		
AAL	\$4293	\$4293	\$5275	-18.6%	-18.6%
BON	3150	3150	3535	-10.9	-10.9
CEN	2918	2918	3017	-3.3	-3.3
FAL	6875	6875	7287	-5.7	-5.7
LCA	2498	1831	1598	+56.3	+14.6
MOH	3118	3097	3078	+1.3	+0.6
NCA	6785	6531	6306	+7.6	+3.6
OZA	4328	4151	3974	+8.9	+4.5
PAC	3939	3939	3954	-0.4	-0.4
PIE	4127	4127	4151	-0.6	-0.6
SOU	3216	3203	3191	+0.8	+0.4
TTA	3792	3157	2915	+30.1	+8.3
WCA	4947	4947	5048	-2.0	-2.0
Total	\$55986	\$52213	\$53329	+1.2%	+2.1%

13/ See Appendix E.

The table shows the total subsidy, both before and after profit-sharing, for each carrier under the plan and compares the subsidy under the plan with the need of the carrier constructed on the basis of its own revenues, expenses, and investment. This table indicates a very close conformance between the subsidy payable under the class rate and needs of the individual carriers. Thus, the deviation between the class rate subsidy and the carriers' needs, range from minus 18.6 percent in the case of Allegheny to a plus 56.3 percent before profit-sharing and 14.6 percent after profit-

sharing for Lake Central. Eliminating Lake Central and Trans-Texas, both of whom present special situations as discussed below, the deviations range from minus 18.6 percent to plus 8.9 percent before and 4.5 percent after profit-sharing for Ozark. We regard such deviations as well within the tolerable area.

The table below shows the rate of return on investment under the class rate formula before and after profit-sharing.

	<u>Rate of Return on Investment Under Class Rate Formula Year Ended June 30, 1960</u>	
	<u>Before Profit-Sharing</u>	<u>After Profit-Sharing</u>
AAL	4.5%	4.5%
BON	7.5	7.5
CEN	7.8	7.8
FAL	8.9	8.9
LCA	62.6	25.7
MOH	9.2	9.1
NCA	15.6	12.9
OZA	14.8	12.7
PAC	9.1	9.1
PIE	9.3	9.3
SOU	13.3	13.1
TTA	34.5	18.7
WCA	8.3	8.3
Average	10.5%	9.2%

It will be seen that, omitting Lake Central and Trans-Texas, the range before profit-sharing is from a low of 4.5 percent return on investment for Allegheny to a high of 15.6 percent for North Central. Trans-Texas and Lake Central show returns before profit-sharing of 34.5 percent and 62.6 percent, respectively. After profit-sharing, the range of returns is from a low of 4.5 percent to a high of 13.1 percent for Southern, including Trans-Texas and Lake Central, and to a high of 25.7 percent including those two carriers.

The range in returns, both before and after profit-sharing, is well within a zone of reasonableness for class rate purposes. It must be borne in mind that no class rate can produce the precise return required by each carrier. Thus, variations in return will be inevitable under even the best formula. It should be noted, of course, that the above analysis does not represent actual results and that the class rate will not be applied retroactively.

Based upon the above retroactive application of the rate, the carrier creating the most severe problem of earnings deficiencies is Allegheny, with a return of 4.5 percent on investment and a theoretical earnings deficiency of \$471,000 after taxes. However, the carrier's return is ample to cover interest expense, leaving something left over as a return on equity. Moreover, the rate is so designed that the carrier can live within the class rate by cutting back its schedules so as to produce (1) a higher over-all load factor, and (2) a higher subsidy rate per available seat mile related to a lower density factor. Thus, it is believed that there is no reason why Allegheny ought not to be able to obtain reasonable earnings under the rate for a future period on a prospective basis. The class rate affords each carrier

advance assurance of the final subsidy support available to it for varying levels of operations and thus enables, and, in fact, encourages the carrier to budget and tailor its operations so as to produce reasonable profits.

The two carriers which appear to stand out from the viewpoint of excess earnings, as noted previously, are Trans-Texas and Lake Central. The low subsidy need of these carriers stems in large part from their low operating costs, and in the case of Lake Central to a load factor which is somewhat higher than normal for a carrier of its modest traffic density. In both cases, the carriers' low costs and excess earnings result to a significant degree from their low investment base, which is composed of

substantially depreciated DC-3 aircraft. However, both carriers have already embarked on a program to equip with more modern aircraft in early 1961. It is anticipated that their 1961 subsidy needs will increase sharply (partially related to recent route awards) and that the rate of return in the future period will be substantially less for both carriers.

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VIII. RATE FORMULA

On the basis of the foregoing findings and conclusions, we find that the fair and reasonable rates of compensation on and after January 1, 1961, to be paid

Allegheny Airlines, Inc.
Bonanza Air Lines, Inc.
Central Airlines, Inc.
Frontier Airlines, Inc.
Lake Central Airlines, Inc.
Mohawk Airlines, Inc.
North Central Airlines, Inc.
Ozark Air Lines, Inc.
Pacific Air Lines, Inc.
Piedmont Airlines
Southern Airways, Inc.
Trans Texas Airways
West Coast Airlines, Inc.

for the transportation of mail by aircraft, the facilities used and useful therefor and the services connected therewith, between the points between which the carrier has been, is presently, or hereafter may be authorized to transport mail by its certificates of public convenience and necessity are the sum of (a) the service mail rates as heretofore and hereafter established for the carrier by Board orders pursuant to section 406(c) of the Act and (b) the subsidy rate for the carrier as set forth in the paragraphs below.

I. The subsidy rate for each carrier for each calendar month on and after January 1, 1961, shall be the rate per available seat mile determined in accordance with Appendix I (attached hereto) on the basis

of the carrier's average number of revenue plane miles flown per station per day in the month; said subsidy rate to be applied to the available seat miles flown in the month, computed in accordance with the provisions and definitions set forth below.

A. The revenue plane miles flown shall be computed on the direct airport-to-airport mileage between the points actually served on each

revenue trip operated over the carrier's routes pursuant to its flight schedules filed with the Board but exclusive of (1) trips flown as extra sections, (2) trips flown pursuant to authority of either certificates of public convenience and necessity or exemption orders issued pursuant to section 416(b) of the Act which do not include authority to transport mail or which expressly include mail authority on a non-subsidy eligibility basis and (3) trips flown over route segments which the Board has authorized the carrier to suspend or the extra mileage involved in serving a point which the Board has authorized the carrier to suspend.

B. The available seat miles flown each month (rounded to the nearest thousand) shall be the product of (1) the revenue plane miles flown computed in accordance with (A) above and (2) the standard number of seats for the respective aircraft types as follows:

<u>Aircraft Type</u>	<u>Standard Seats</u>
DC-3	24
CV-240; F-27; M-202	40
CV-340; CV-440; M-404	44
CV-540	52

C. The term "station" shall be deemed to be the monthly average number of airports operated for the carrier, computed on an airport-day basis, with each airport given weight proportional to the number of days operated during the month pursuant to Board authorizations; provided, however, that any airport serving a point which the Board has authorized the carrier to suspend shall not be included in the computation of airports operated. Airports served a full month shall be given

a weight equal to the number of days in the month; airports served less than a full month shall be given a weight equal to the number of days service was authorized. The aggregate number of airport-days shall be divided by the appropriate number of days in the month to derive the weighted number of airports operated. The computation shall be carried out to one decimal place.

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D. In computing the revenue plane miles flown per station per day for each month, the number of days in the month shall be based on the number of days in the calendar month exclusive of days on which operations are completely suspended due to a strike or similar work stoppage. On any days of partial reduction of operations due to strikes or similar work stoppage, when the revenue plane miles flown by the carriers are less than 90 percent of the revenue plane miles scheduled to be flown for such days, such days shall be counted as a reduced number of days to be arrived at by multiplying the number of such days by the ratio of (1) the revenue plane miles flown on such days divided by (2) the product of the revenue plane miles scheduled to be flown on such days ^{13a/} times the system average performance factor of the carrier during the corresponding month or months of the prior year.

E. The subsidy otherwise payable to the carrier under this Section (I) above shall be reduced by the amount of any adjusted annual capital gain in accordance with the provisions set forth in Appendix B to Order E-14104, dated June 24, 1959, as such Appendix B may be amended from time to time, and said Appendix B is hereby incorporated herein by reference.

F. The subsidy otherwise payable to the carrier under this Section (I) above shall be subject to reduction in accordance with the Profit Sharing terms and conditions specified in (II) below.

II. The annual subsidy otherwise due and payable to each carrier pursuant to (I) above, shall be subject to reduction to the extent that the

carrier's earnings for calendar year 1961 and each succeeding calendar year exceed the carrier's fair and reasonable differentiated rate of return, in

13a / Based on the carrier's official schedules on file with the Board on the last day prior to the work stoppage.

accordance with the provisions set forth below. In the event that this class rate terminates prior to the last day of a calendar year and is not superseded by a class rate containing profit-sharing provisions, the subsidy otherwise due and payable to each carrier pursuant to Section I for any such period of less than a calendar year shall be subject to reduction in like manner, provided that the results of the carrier for such period shall be adjusted to eliminate seasonal distortions.

A. Each carrier's fair and reasonable differentiated rate of return shall be the weighted average rate of return arrived at by applying rates of 21.35%, 7.5% and 5.5% to the common stock equity, preferred stock equity and debt components of recognized investment, respectively; provided that (1) the maximum rate of return computed in accordance with the preceding portion of this paragraph shall not exceed 12.75% (after applicable income taxes) and shall not be less than 9.00% (after applicable income taxes), and (2) in no event shall the fair and reasonable differentiated rate of return be less than the equivalent of three cents (after applicable income taxes) per revenue plane mile flown (in accordance with the definition of revenue plane miles flown as defined in IA, above).

B. In any case where a carrier's annual earnings (after applicable income taxes) exceed its fair and reasonable differentiated rate of return, such carrier shall refund a portion of such profits to the extent indicated in the Table below to the Board as subsidy not due the carrier:

<u>Rate of Return (After Taxes)</u>	<u>Percentage of Profits Refunded by Carrier</u>
0% to D ^{14/}	0%
D to 15%	50%
Over 15%	75%

^{14/} D represents the fair and reasonable differentiated rate of return for each carrier as defined in IIA, above.

C. In applying the Table in B above, the amounts due to be refunded to the Board in any calendar year shall be reduced by the amount of any earnings deficiency of the carrier in the two preceding calendar years (exclusive of periods prior to January 1, 1961). An earnings deficiency is defined as the amount by which the carrier's earnings (after applicable income taxes) in a calendar year are less than the fair and reasonable differentiated rate of return specified in IIA above.

III. In applying the provisions of II, above, the revenues and other income items, expenses, investment and income taxes shall be determined in accordance with the provisions of this Section III.

A. Revenues

1. The revenues shall be those reported by each carrier on its Form 41 reports to the Board, provided that such reports are consistent with the requirements of the Act and the Board's Regulations (particularly Part 241 and the Uniform System of Accounts for Air Carriers) and that such reports reflect accounting practices consistent with the carrier's practices in reports for prior periods, except in cases where the carrier has obtained Board approval for change in such accounting practices.

2. The revenues in reports not complying with 1, above, shall be adjusted to comply therewith in applying the provisions of II, above.

3. Revenues reported from non-transport activities or from transactions with affiliates shall be excluded unless

the profit (after income taxes) to the carrier from such activities exceeds the fair and reasonable differentiated rate of return for the carrier for air transport operations, in which case such excess shall be utilized for the purpose of II, above.

For the purpose of this entire Section III, the term affiliate (or affiliated) shall be deemed to include any "associated company" as defined at page 31.2 of the Uniform System of Accounts or any relationship defined as "affiliated" in Part 261.8(b) of the Board's Economic Regulations, as amended.

B. Operating Expenses

1. The operating expenses shall be those reported by each carrier on its Form 41 reports to the Board provided that such reports are consistent with the requirements of the Act and the Board's Regulations (particularly Part 241 thereof and the Uniform System of Accounts) and that such reports reflect accounting practices consistent with the carrier's accounting in previous periods, except in cases where the carrier has obtained Board approval for change in such accounting practice, and provided further that reporting and accounts not complying with this paragraph 1 shall be adjusted to comply therewith in applying the provisions of II, above.

2. The operating expenses otherwise reported or determined in accordance with paragraph 1, above, shall be subject to the conditions set forth below.

3. Non-allowable expenses - The following operating expense items shall not be recognized and shall be disallowed:

a. Any reported expense which does not comply with the Act, or any other provisions of law, or regulation of the Board or other agency of Government;

b. Fines or other similar penalties accrued, or paid, as the result of violation of law or in violation of any association rule or by-law;

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c. All financing costs and costs related to financing;

d. Lobbying costs;

e. Compensation, in any form whatsoever, paid directly or indirectly to or on behalf of any officer, director, or employee, of the carrier in excess of \$25,000 per annum;

f. Any payment made directly or indirectly, in any form whatsoever, to or on behalf of any officer, director or employee of the carrier, or to or on behalf of any stockholder owning in excess of a 1 percent stock interest, unless such payment is reasonable and directly related to the air transportation services of the carrier;

g. Any payment to directors, officers or employees in the nature of bonuses related to profits or representing a sharing of profits;

h. Any form of dues (including initiation fees) expensed on behalf of the carrier or any officer or director, unless such dues are for membership in a business, professional or trade organization;

i. Any self-insurance or other accruals requiring Board approval of the basis of accrual, unless approved by the Board or by the Board's staff under delegated authority;

j. Expenses incurred and accrued for proceedings in which the carrier is an unsuccessful applicant for an exemption or route award, or is an intervenor; Provided further that during its prosecution of an exemption or route award expenses incurred by the carrier for that

purpose shall be held in suspense, for the purpose of this order, pending final decision of the Board, and if the carrier receives an award thereunder the expenses related to the carrier's successful prosecution of its case shall be recognized by amortization over a period of 5 years or the period of the award, if shorter, such

amortization to commence as of the date of institution of the service provided pursuant to the Board's final decision in the exemption or route proceedings; ^{17/}—

k. Expenses in proceedings before the Board for witnesses other than the carrier's personnel or consultants hired by the carrier;

l. Contributions on behalf of the carrier for charitable or similar purposes;

m. Premiums for life insurance on the life of any officer, director or employee where the company is a named beneficiary.

n. Expenses incurred in non-transport activities except to the extent that such expenses are offset against revenues from such activities in accordance with III A 3 above.

4. The following expenses shall be recognized to the extent indicated:

a. Expenses incurred by the carrier in dealings with an affiliate (including a separately operated division) shall be recognized only to the extent that the charges by the affiliate are at cost, including a proper share of overhead and a capital cost not exceeding the level of the air carrier's own fair and reasonable differentiated rate of return;

b. Costs which result from transactions not at arms length, dealings involving conflicts of interest, or involving fraud

17/ In cases covered by this proviso clause where the Board prior to January 1, 1961, has established a final subsidy rate which would otherwise be applicable on and after January 1, 1961, amortization shall be recognized as per such final rate order.

on the part of the air carrier, its personnel or any person under the carrier's control shall be recognized only to the extent that such costs do not exceed reasonable levels;

c. In case the carrier enters into a sale of equipment, with a provision for lease-back of such equipment or similar equipment, any cost exceeding that which would have been incurred had such sale and lease-back not occurred will not be recognized.

5. The depreciation expense to be recognized for flight equipment (including hulls and all related flight components) shall be subject to the following additional special rules and conditions:

a. For flight equipment acquired and placed into service prior to January 1, 1961, the recognizable expense shall be based on the book value recorded as of December 31, 1960, provided that such value does not exceed the depreciated original cost of such equipment to the air carrier;

b. For flight equipment acquired and placed into service on or after January 1, 1961, the recognizable expense shall be based on the depreciable original cost of such equipment (including capitalized interest) to the air carrier;

c. The service lives and residual values for flight equipment (including hulls and all related components) shall be as set forth in the following table:

<u>Equipment Type</u>	<u>Service Life</u>	<u>Residual Value</u>
DC-3	3 years	10%
all other piston-powered aircraft	7 years	15%
turbine-powered aircraft	10 years	15%

d. The service life for each aircraft type shall be deemed to commence as of the date of its introduction into regularly scheduled service, provided that the remaining service life for aircraft placed into service prior to January 1, 1961, shall be computed by subtracting from the years of service life set out in the table above the periods prior to January 1, 1961, for which depreciation has been accrued by the air carrier for such flight equipment, and the remainder of the depreciable value so derived shall be spread out equally each month from January 1, 1961 forward; 18/

e. For the purpose of this paragraph 5, the otherwise recognizable depreciable cost for aircraft hulls and engines shall be reduced by the value of the so-called "built-in-overhaul," such value to be determined at a reasonable level consistent with prior and anticipated experience; Provided, however, that where aircraft are maintained on a phase or pattern overhaul basis, the depreciable cost shall be reduced by only 50 percent of the value of the "built-in-overhaul" plus the value of the hours remaining to the next phase or pattern overhaul; Provided further that maintenance charges will be recognized consistent with the built-in-overhaul principle, and that accruals to a reserve for future overhauls will not be recognized.

18/ Where a final rate has been established for the carrier prior to January 1, 1961 the "remaining service life" shall be based on the depreciation rates recognized in such final order (or orders).

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C. Investment

1. Subject to the same requirements as to compliance with the Act and the Board's Regulations, as set forth in A and B, above, the investment shall be the average of the balance sheets reported for the four quarters of the calendar year, for which Section II, above, is being applied, and the year end balance sheet for the immediately preceding year, with one-half weight accorded the opening and closing balance sheets.

2. The investment shall be subject to the additional special rules and conditions set forth below:

- a. Notes payable due beyond 90-days shall be treated as long-term debt;
- b. Non-operating property shall be excluded;
- c. The air carrier's investment in any affiliated or non-transport activity shall be recognized only in the event that the profits (after income taxes) reported by the air carrier from such company or activity exceed the fair and reasonable differentiated return of the air carrier and such profits are utilized to reduce the air carrier's subsidy;
- d. The investment shall not include the cash or other value of any life insurance policy covering any company executive;
- e. The investment shall not include equipment replacement funds derived from sale of flight equipment, but such funds shall be recognized only when re-invested in property which is productive in the carrier's transport operations;
- f. The investment shall not include equipment purchase deposits, capitalized organizational expense, capital stock

expense, unamortized discount and expense on debt, and/or special funds such as sinking funds as specified in Account 1550 in the Uniform Manual of Accounts;

g. Working capital in excess of the equivalent of 3 months' operating expenses, exclusive of depreciation and amortization, shall be excluded;

h. Reserves accrued through charges to operating expense will be treated as a current liability for the purpose of this paragraph C;

i. Construction work in progress shall be recognized only to the extent that capitalized interest on such item is not claimed by the carrier;

j. The computation of working capital related to periods prior to January 1, 1961 shall reflect the subsidy payable to the air carrier pursuant to the most recent Board order dealing with the carrier's subsidy for such period, but for periods commencing January 1, 1961, accruals for each balance sheet date shall be made pursuant to the rate established by this Order.

D. Other Income and Non-operating Expenses - In applying Section II, above, all income to the carrier (other than capital gains on flight equipment qualifying pursuant to Section 406(d) of the Act and the Board's Regulations thereunder) shall be included whether such income is recorded as revenue, non-operating income and/or Special Income; but only the following classes of non-operating expenses shall be recognized:

1. Capital losses on ground equipment; and

2. Non-routine foreign exchange adjustments.

E. Where an adjustment is required and effected pursuant to the provisions of paragraph III A or B or C or D above, such appropriate adjustments shall be made for the purpose of all other provisions of this Section III where sound accounting practice and consistency so require.

F. Income Taxes - Federal and State income taxes shall be determined on the basis of the carrier's income tax returns for each year as submitted to the taxing authorities, with such amendments or revisions (including tax carry-back and carry forward credits) as may have been filed as of the date of the final determination of excess profits (or an earnings deficiency) under this Order, Provided, however, that for carriers whose tax returns are filed for a 12 month period not coinciding with a calendar year, a pro forma tax return will be required to be submitted for the calendar year, which return shall be prepared on bases consistent with the returns of that carrier filed for the latest fiscal year with the appropriate tax authorities. ^{19/}

G. The refund otherwise due and payable to the Government pursuant to Section II shall be increased by the amount of the income tax savings estimated to accrue to the carrier as a result of such refund.

An appropriate order will be entered.

Boyd, Chairman, Gurney, Vice Chairman, Minetti, Gilliland and Bragdon, Members of the Board, concurred in the above Statement.

^{19/} A reconciliation of such pro forma return with the carrier's reported operating results will be required.

[48]

Order No. E-16380

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D. C.
on the 16th day of February, 1961

- - - - -
In the Matter of the Local :
Service Class Subsidy Rate : Docket No. 12004
Investigation :
- - - - -

ORDER TO SHOW CAUSE

The Board having considered all of the information and data set forth or specifically referred to in the Statement of Provisional Findings and Conclusions ^{1/} (hereinafter referred to as the "Statement"), which is attached hereto and incorporated herein, and having on the basis thereof made the provisional findings and conclusions and determined the rates specified in the Statement;

IT IS ORDERED, That each of the parties to these proceedings is directed to show cause why the Board should not adopt the findings and conclusions specified in the Statement and fix, determine, and publish the final rates specified in the Statement as the fair and reasonable rates of compensation to be paid for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith over the entire system of each carrier party to these proceedings.

IT IS FURTHER ORDERED, That all further procedure herein shall be in accordance with the Rules of Practice, particularly Rule 302, et seq., and if there is any objection to the rates or any other provision specified in the Statement, notice thereof shall be filed within 10 days, and, if notice is filed, written answer and supporting documents shall be filed within 30 days, after the date of service of this order.

IT IS FURTHER ORDERED, That, if notice of objection is not filed within 10 days, or, if notice is filed, answer is not filed within 30 days, after service of this order, all parties shall be deemed to have waived the right to a hearing and all other procedural steps short of a final decision by the Board, and the Board may enter an order fixing the rates specified in the Statement; Provided, that if notice of objection and answer

1/ All forms, reports, schedules, and tariffs filed with the Board by each of the carriers party to these proceedings, to the date of the Board's final decision, and the official mileage record of the Board, are incorporated into the record of these proceedings.

are filed by any carrier or carriers, the Board may enter an order fixing the rates specified in the Statement for such carriers as have not filed notice of objection or, having filed such notice, have not filed timely answer.

IT IS FURTHER ORDERED, That, in accordance with the order instituting these proceedings (Order E-16173, December 23, 1960) if answer is filed, the issues shall be confined to the matter of establishing a class rate for the local service carriers, i. e., whether such a class rate shall be established and, if so, the fair and reasonable class rate under Section 406 of the Act.

IT IS FURTHER ORDERED, That this order and the attached Statement of Provisional Findings and Conclusions be served upon all parties to this proceeding.

By the Civil Aeronautics Board:

/s/ Robert C. Lester

Robert C. Lester
Secretary

(SEAL)

LOCAL SERVICE CLASS SUBSIDY RATE

Overall Summary
Hypothetical Application of Class Rate by Carrier
Twelve Months Ended June 30, 1960

	<u>Allegheny</u>	<u>Bonanza</u>	<u>Central</u>	<u>Frontier</u>	<u>Lake Central</u>	<u>Mohawk</u>	<u>North Central</u>	<u>Ozark</u>	<u>Pacific</u>	<u>Piedmont</u>	<u>Southern</u>	<u>Trans-Texas</u>	<u>West Coast</u>	<u>Total</u>
Plane Miles Flown: ^{a/}	7,324,204	4,592,022	4,010,479	9,587,085	3,688,677	5,517,567	14,140,649	8,879,354	6,031,455	7,235,396	5,263,847	6,196,354	6,536,981	71,004,370
Annual Daily	20,011	12,547	10,958	26,194	10,078	15,075	38,636	24,261	16,479	19,769	14,382	22,394	17,861	243,645
Average Stations	29.3	25.0	35.0	68.4	29.0	20.4	59.8	44.4	25.4	31.6	36.5	40.4	42.9	488.1
Daily Miles per Station	683	502	313	383	348	759	646	546	649	626	394	554	416	509
Subsidy rate ^{b/}	1.6691¢	2.0644¢	3.0320¢	2.6120¢	2.8220¢	1.5426¢	1.7647¢	1.9412¢	1.7566¢	1.8211¢	2.5460¢	1.9276¢	2.4140¢	
Available Seat Miles (000)	257,180	152,583	96,251	263,199	88,528	202,099	384,484	222,943	224,226	226,648	126,332	196,712	204,949	2,546,134
Computed Subsidy (000)	\$4,293	\$3,150	\$2,918	\$6,875	\$2,498	\$3,118	\$6,785	\$4,328	\$3,939	\$4,127	\$3,216	\$3,792	\$4,947	\$53,986
Break-Even Need ^{c/} (000)	\$3,553	\$2,185	\$2,789	\$6,135	\$1,430	\$1,770	\$5,533	\$3,189	\$2,964	\$3,209	\$2,643	\$2,460	\$4,192	\$42,052
Income before Taxes (000)	\$ 740	\$ 965	\$ 129	\$ 740	\$1,068	\$1,348	\$1,252	\$1,139	\$ 975	\$ 918	\$ 573	\$1,332	\$ 755	\$11,934
Profit-Sharing ^{d/} (000)	-	-	-	-	\$ 667	\$ 21	\$ 254	\$ 177	-	-	\$ 13	\$ 635	-	\$ 1,767
Taxes ^{e/} (000)	\$ 266	\$ 381	\$ 55	\$ 277	\$ 178	\$ 510	\$ 410	\$ 440	\$ 360	\$ 301	\$ 270	\$ 335	\$ 249	\$ 4,032
Income After Profit-Sharing and Taxes Dollars (000)	\$ 474	\$ 584	\$ 74	\$ 463	\$ 223	\$ 817	\$ 588	\$ 522	\$ 615	\$ 617	\$ 290	\$ 362	\$ 506	\$ 6,135
% Investment	4.5	7.5	7.8	8.9	25.7	9.1	12.9	12.7	9.1	9.3	13.1	18.7	8.3	9.2

^{a/} In revenue, scheduled service, excluding extra sections, per Form 41. See Appendix F.

^{b/} Per available seat mile per Appendix I.

^{c/} Per Appendix E.

^{d/} Per Appendix C.

^{e/} Per Appendix D.

LOCAL SERVICE CLASS SUBSIDY RATE

Overall Summary
 Application of Class Rate by Carrier
 to Forecast Operations for Calendar Year 1961

	<u>Allegheny</u>	<u>Bonanza</u>	<u>Central</u>	<u>Frontier</u>	<u>Lake Central</u>	<u>Mohawk</u>	<u>North Central</u>	<u>Ozark</u>	<u>Pacific</u>	<u>Piedmont</u>	<u>Southern</u>	<u>Irons Texas</u>	<u>West Coast</u>	Total
Plane miles flown: Annual Daily	10,518,620 28,818	4,371,348 11,976	6,107,975 16,734	9,009,175 24,683	7,427,160 20,348	6,455,000 17,685	14,578,000 40,214	8,918,609 24,435	5,820,000 15,945	7,161,505 19,621	9,053,275 24,803	8,039,473 22,026	6,777,904 19,570	104,338,044 285,858
Average stations Daily Miles per station	37.3 773	19.5 614	46.0 364	64.0 384	41.7 188	25.0 707	73.4 548	45.0 513	25.0 438	33.2 591	50.0 495	38.0 580	45.0 413	543.1 525 [51]
Subsidy rate	1.4748 ^a	1.8567 ^a	2.7260 ^a	2.5940 ^a	2.1035 ^a	1.6125 ^a	1.9355 ^a	1.9495 ^a	1.7868 ^a	1.9054 ^a	2.0812 ^a	1.9120 ^a	2.4320 ^a	
Available Seat Miles (000) Computed Subsidy (000)	416,373 \$ 6,141	174,854 \$3,247	163,194 \$4,449	271,184 \$7,035	206,372 \$4,341	253,388 \$4,086	420,512 \$8,139	234,613 \$4,574	228,680 \$4,086	229,034 \$4,354	217,279 \$4,522	222,567 \$4,257	220,713 \$5,368	3,258,863 \$54,609

^a/ Per Appendix H.
^b/ As forecast by carriers.
^c/ Per Appendix I.

APPENDIX B

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LOCAL SERVICE CLASS SUBSIDY RATE

Calculation of Profit Sharing by Carrier
 Hypothetical Application of Class Rate
 Twelve Months Ended June 30, 1960

	<u>Allegheny</u>	<u>Bonanza</u>	<u>Central</u>	<u>Frontier</u>	<u>Lake Central</u>	<u>Mohawk</u>	<u>North Central</u>	<u>Ozark</u>	<u>Pacific</u>	<u>Piedmont</u>	<u>Southern</u>	<u>Trans-Texas</u>	<u>West Coast</u>	<u>Total</u>
Investment ^{a/} (000)	\$10,505	\$7,768	\$ 952 ^{d/}	\$5,182	\$ 668 ^{d/}	\$8,979	\$4,542	\$4,114	\$6,778	\$6,603	\$2,225	\$1,932 ^{d/}	\$6,103	\$66,551
Return element ^{b/} (000)	\$ 945	\$ 769	\$ 121	\$ 661	\$ 111 ^{c/}	\$ 808	\$ 481	\$ 438	\$ 621	\$ 628	\$ 284	\$ 246	\$ 554	\$ 6,667
Percent of investment	9.00%	9.90%	14.05%	12.75%	13.03%	9.00%	10.50%	10.64%	9.17%	9.51%	12.75%	13.09%	9.08%	10.02%
Income after tax ^{c/} (000)	\$ 474	\$ 584	\$ 74	\$ 463	\$ 543	\$ 327	\$ 710	\$ 607	\$ 615	\$ 617	\$ 296	\$ 667	\$ 506	\$ 6,983
Percent of investment	4.51%	7.52%	7.77%	8.93%	62.6%	9.21%	15.63%	14.75%	9.07%	9.34%	13.30%	34.52%	6.29%	10.49%
Profit sharing to Gov't. (000)	-	-	-	-	\$ 0	\$ 0	\$ 0	\$ 0	-	-	\$ 0	\$ 0	-	\$ 0
To return element "D" - 0%	-	-	-	-	\$ 10	\$ 10	\$ 100	\$ 85	-	-	\$ 6	\$ 22	-	\$ 233
"D" to 15%	-	-	-	-	\$ 310	-	\$ 22	-	-	-	-	\$ 263	-	\$ 615
Over 15%	-	-	-	-	\$ 320	\$ 10	\$ 122	\$ 85	-	-	\$ 6	\$ 305	-	\$ 648
Total	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Tax reduction on Gov't. share (000)	-	-	-	-	\$ 347	\$ 11	\$ 132	\$ 92	-	-	\$ 7	\$ 330	-	\$ 919
Total profit sharing (000)	-	-	-	-	\$ 667	\$ 21	\$ 254	\$ 177	-	-	\$ 13	\$ 635	-	\$ 1,767

^{a/} As of June 30, 1960. See Appendix E.^{b/} Per Appendix E.^{c/} Before profit sharing. See Appendix D.^{d/} Computed to equate return with 12.75%.^{e/} Three cents per mile carrier.

LOCAL SERVICE CLASS SUBSIDY RATE

Calculation of Federal Income Taxes
Hypothetical Application of Class Rate
Twelve Months Ended June 30, 1960

(In Thousands)

	<u>Income Before Tax & Profit Sharing</u> ^{a/}	<u>Reported Interest Expense</u>	<u>Taxable Income</u>	<u>Income Tax @ 52% less \$5,500</u>	<u>Tax Reduction for Profit Sharing</u> ^{b/}	<u>Total Income Tax</u>
Allegheny	\$ 740	\$ 218	\$ 522	\$ 266	\$ -	\$ 266
Bonanza	965	222	743	381	-	381
Central	129	12	117	55	-	55
Frontier	740	197	543	277	-	277
Lake Central	1,068	47	1,021	525	347	178
Mohawk	1,348	336	1,012	521	11	510
North Central	1,252	200	1,052	542	132	410
Ozark	1,139	107	1,032	532	92	440
Pacific	975	271	704	360	-	360
Piedmont	918	328	590	301	-	301
Southern	573	30	543	277	7	270
Trans Texas	1,332	43	1,289	665	330	335
West Coast	<u>755</u>	<u>265</u>	<u>490</u>	<u>249</u>	<u>-</u>	<u>249</u>
Total	\$11,934	\$2,276	\$9,658	\$4,951	\$919	\$4,032

a/ Per Appendix A

b/ See Appendix C

LOCAL SERVICE CLASS SUBSIDY RATE

Allegheny Airlines, Inc.
 Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Breakeven Need</u>
Operating results, as reported 12-months 6/30/60	\$8,753,041	\$13,103,470	\$ 4,350,429
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per passenger	743,958		- 743,958
Accrued vacation expense		-18,000	- 18,000
Entertainment expense		- 9,000	- 9,000
Amortization		-18,000	- 18,000
Executive salaries in excess of \$25,000		- 8,000	- 8,000
Operating results, as adjusted	<u>\$9,496,999</u>	<u>\$13,050,470</u>	<u>\$ 3,553,471</u>
Investment as of June 30, 1960	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported, June 30, 1960	\$8,218,802	\$ 145,341	\$ 8,364,143
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	579,131		579,131
Unamortized discount and expense on debt	- 463,720		- 463,720
Estimated additional past period mail pay		1,929,000	1,929,000
Accrued vacation liability		126,858	126,858
Sub-total	<u>\$8,334,213</u>	<u>\$ 2,201,199</u>	<u>\$10,535,412</u>
Debt-equity ratio	79.11%	20.89%	
Adjustments Prorated:			
Equipment deposits	<u>- 24,126</u>	<u>- 6,371</u>	<u>- 30,497</u>
Investment as adjusted	<u>\$8,310,087</u>	<u>\$ 2,194,828</u>	<u>\$10,504,915</u>
Differentiated rates of return	5.50%	21.35%	
Return on investment	<u>\$ 457,055</u>	<u>\$ 468,596</u>	<u>\$ 925,651</u>
Return as percent of investment			8.81%
To provide minimum return of 9%			945,442
Tax, reflecting interest expense of \$217,664			776,967
Total return and tax			<u>\$ 1,722,409</u>
Subsidy requirement: breakeven need, return and tax			
Dollars			<u>\$ 5,275,880</u>
Per Available seat mile			<u>2.0514¢</u>

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LOCAL SERVICE CLASS SUBSIDY RATE

Bonanza Air Lines, Inc.
 Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

Appendix E
 Page 2 of 13

	<u>Revenues</u>	<u>Expenses</u>	<u>Break-even Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	\$4,589,015	\$ 7,196,069	\$ 2,607,054
<u>Adjustments:</u>			
Fare increase, 2 1/2% plus 90¢ per passenger	326,363		- 326,363
Accrued vacation expense		-39,000	- 39,000
Depreciation		-36,000	- 36,000
Entertainment expense		-19,000	- 19,000
Out of period expense		- 1,000	- 1,000
Misc. expenses		- 1,000	- 1,000
<u>Operating results, as adjusted</u>	<u>\$4,915,378</u>	<u>\$ 7,100,069</u>	<u>\$ 2,184,691</u>
<u>Investment as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
<u>As reported, June 30, 1960</u>	<u>\$3,858,173</u>	<u>\$ 1,691,312</u>	<u>\$ 5,549,485</u>
<u>Adjustments Directly Assigned:</u>			
Transfer of 75% of notes payable to long-term debt	305,659		305,659
Debt on F-27s in service	1,486,501		1,486,501
Estimated additional past period mail pay		346,000	346,000
Accrued vacation liability		130,701	130,701
Sub-total	<u>\$5,650,333</u>	<u>\$ 2,168,013</u>	<u>\$ 7,818,346</u>
Debt-equity ratio	72.27%	27.73%	
<u>Adjustments Prorated:</u>			
Nonoperating property	-35,947	-13,793	- 49,740
Equipment deposits	- 723	- 277	- 1,000
	<u>-36,670</u>	<u>-14,070</u>	<u>- 50,740</u>
<u>Investment, as adjusted</u>	<u>\$5,613,663</u>	<u>\$ 2,153,943</u>	<u>\$ 7,767,606</u>
Differentiated rates of return	5.50%	21.35%	
<u>Return on investment</u>	<u>\$ 308,751</u>	<u>\$ 459,867</u>	<u>\$ 768,618</u>
Return as percent of investment			9.90%
Tax, reflecting interest expense of \$221,580			<u>\$ 581,166</u>
Total return and tax			<u>\$ 1,349,784</u>
<u>Subsidy requirement: break-even need, return and tax</u>			
Dollars			<u>\$ 3,534,475</u>
Per available seat-mile			<u>2.3164¢</u>

LOCAL SERVICE CLASS SUBSIDY RATE

Central Airlines, Inc.
Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Break-even Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	\$2,585,801	\$5,616,254	\$3,030,453
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per passenger	203,566		- 203,566
Entertainment expense		- 9,000	- 9,000
Overhaul accounting		-11,000	- 11,000
Misc.		-10,000	- 10,000
Adv.-Trade agreements		- 7,000	- 7,000
Amortization		- 1,000	- 1,000
Operating results, as adjusted	<u>\$2,789,367</u>	<u>\$5,578,254</u>	<u>\$2,788,887</u>
<u>Investment as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported June 30, 1960		\$ 237,074	\$ 237,074
Adjustments Directly Assigned:			
Transfer of 75% notes payable to long-term debt	\$ 202,500		202,500
Estimated additional past period mail pay		<u>425,000</u>	<u>425,000</u>
Sub-total	<u>\$ 202,500</u>	<u>\$ 662,074</u>	<u>\$ 864,574</u>
Debt-equity ratio	23.42%	76.58%	
Adjustments Prorated:			
Nonoperating deposits	-12	- 41	- 53
Equipment deposits	-74	-240	-314
	<u>-86</u>	<u>-281</u>	<u>-367</u>
Investments, as adjusted	<u>\$ 202,414</u>	<u>\$ 661,793</u>	<u>\$ 864,207</u>
Differentiated rates of return	5.50%	21.35%	
<u>Return on investment</u>	<u>\$ 11,133</u>	<u>\$ 141,293</u>	<u>\$ 152,426</u>
Return as percent of investment			17.64%
To provide minimum of 3¢ per mile			121,410
Tax reflecting interest expense of \$12,307			<u>106,737</u>
Total return and tax			<u>\$ 228,147</u>
Subsidy requirement: break-even need, return and tax	Dollars		<u>\$3,017,034</u>
Per available seat-mile			<u>3.1345¢</u>

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LOCAL SERVICE CLASS SUBSIDY RATE

Frontier Airlines, Inc.
 Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Breakeven Need</u>
Operating results, as reported 12-months 6/30/60	\$6,874,252	\$13,601,420	\$6,727,168
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per passenger	447,025		- 447,025
Accrued vacation expense		- 91,000	- 91,000
Entertainment expense		- 46,000	- 46,000
Amortization		- 7,000	- 7,000
Operating results, as adjusted	\$7,321,277	\$13,457,420	\$6,136,143
Investments as of June 30, 1960	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported, June 30, 1960	\$2,196,564	\$ 1,186,347	\$3,382,911
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	558,576		558,576
Estimated additional past period mail pay		997,000	977,000
Accrued vacation liability		286,377	286,377
Sub-total	<u>\$2,755,140</u>	<u>\$ 2,449,724</u>	<u>\$5,204,864</u>
Debt-equity ratio	52.93%	47.07%	
Equipment deposits prorated	<u>-12,174</u>	<u>-10,826</u>	<u>-23,000</u>
Investment, as adjusted	<u>\$2,742,966</u>	<u>\$ 2,438,898</u>	<u>\$5,181,864</u>
Differentiated rates of return	5.50%	21.35%	
<u>Return on Investment</u>	<u>\$ 150,863</u>	<u>\$ 520,705</u>	<u>\$ 671,568</u>
Return as percent of investment			12.96%
To provide maximum return of 12.75%			660,688
Tax, reflecting interest expense of \$196,648			<u>491.252</u>
Total return and tax			<u>\$1,151,940</u>
Subsidy requirement: breakeven need, return and tax			<u>\$7,288,083</u>
Dollars			<u>2.7690¢</u>
Per available seat-mile			

LOCAL SERVICE CLASS SUBSIDY RATE

Lake Central Airlines, Inc.
Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Break-even Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	\$2,992,072	\$4,724,472	\$1,732,400
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per psgr.	284,003		- 284,003
Miscellaneous expense		-9,000	- 9,000
Executive salaries		-4,000	- 4,000
Entertainment expense		-3,000	- 3,000
Depreciation		-2,000	- 2,000
<u>Operating results, as adjusted</u>	<u>\$3,276,075</u>	<u>\$4,706,472</u>	<u>\$1,430,397</u>
<u>Investment as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
<u>As reported, June 30, 1960</u>	<u>\$ 400,000</u>	<u>\$ 380,577</u>	<u>\$ 780,577</u>
Adjustments Directly Assigned:			
Transfer of 75% notes payable to long-term debt	198,313		198,313
Unamortized discount and expense on debt	-7,932		- 7,932
Estimated Additional past period mail pay		-71,000	- 71,000
Sub-total	<u>\$ 590,381</u>	<u>\$ 309,577</u>	<u>\$ 899,958</u>
Debt-equity ratio	<u>65.60%</u>	<u>34.40%</u>	
Equipment deposits prorated	<u>-33,093</u>	<u>-17,353</u>	<u>-50,446</u>
<u>Investment as adjusted</u>	<u>\$ 557,288</u>	<u>\$ 292,224</u>	<u>\$ 849,512</u>
Differentiated rates of return	<u>5.50%</u>	<u>21.35%</u>	
<u>Return on Investment</u>	<u>\$ 30,651</u>	<u>\$ 62,390</u>	<u>\$ 93,041</u>
Return as percent of investment			10.95%
To provide minimum of 3¢ permile			110,722
Tax, reflecting interest expense of \$46,999			57,575
Total return and tax			<u>\$ 168,297</u>
<u>Subsidy requirement: break-even need, return and tax</u>			
Dollars			<u>\$1,598,694</u>
Per available seat-mile			<u>1.8059¢</u>

LOCAL SERVICE CLASS SUBSIDY RATE

Mohawk Airlines, Inc.
 Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Break-even Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	\$8,960,509	\$11,480,165	\$2,519,656
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per psgr.	696,434		- 696,434
Executive salaries		- 26,000	- 26,000
Amortization		- 23,000	- 23,000
Out of period		+ 10,000	+ 10,000
Bad debts		- 8,000	- 8,000
Entertainment expenses		- 6,000	- 6,000
<u>Operating results, as adjusted</u>	<u>\$9,656,943</u>	<u>\$11,427,165</u>	<u>\$1,770,222</u>
<u>Investments as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported, June 30, 1960	\$7,478,250	\$ 200,527	\$7,678,777
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	825,000		825,000
Estimated additional past period mail pay		843,000	843,000
Unamortized discount and expense on debt	- 348,962		- 348,962
Sub-total	\$7,954,288	\$ 1,043,527	\$8,997,815
Debt-equity ratio	88.40%	11.60%	
Adjustments Prorated:			
Equipment deposits	- 694	- 91	- 785
Officers' notes	- 15,470	- 2,030	- 17,500
Mohawk Air Service	- 354	- 46	- 400
	<u>- 16,518</u>	<u>- 2,167</u>	<u>- 18,685</u>
<u>Investment, as adjusted</u>	<u>\$7,937,770</u>	<u>\$ 1,041,360</u>	<u>\$8,979,130</u>
Differentiated rates of return	5.50%	21.35%	
<u>Return on investment</u>	<u>436,577</u>	<u>222,330</u>	<u>\$ 658,907</u>
Return as percent of investment			7.34%
To provide minimum return of 9%			808,122
Tax, reflecting interest expense of \$336,021			499.984
Total return and tax			<u>\$1,308,106</u>
Subsidy requirement: break-even need, return and tax			
Dollars			\$3,078,328
Per available seat-mile			<u>1.5232¢</u>

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LOCAL SERVICE CLASS SUBSIDY RATE

North Central Airlines, Inc.
Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Breakeven Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	<u>\$13,464,793</u>	<u>\$20,368,104</u>	<u>\$6,903,311</u>
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per passenger	1,157,152		-1,157,152
Depreciation		- 121,000	- 121,000
Entertainment expenses		- 36,000	- 36,000
Executive salaries		- 30,000	- 30,000
Amortization		- 25,000	- 25,000
Accrued vacation expense		- 1,000	- 1,000
<u>Operating results as adjusted</u>	<u>\$14,621,945</u>	<u>\$20,155,104</u>	<u>\$5,533,159</u>
<u>Investment as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported, June 30, 1960	\$ 2,598,027	\$ 497,161	\$3,095,188
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	565,710		565,710
Unamortized discount and expense on debt	- 62,996		- 62,996
Estimated additional past period mail pay		966,000	966,000
Accrued vacation liability		1,400	1,400
Sub-total	<u>\$ 3,100,741</u>	<u>\$ 1,464,561</u>	<u>\$4,565,302</u>
Debt-equity ratio	67.92%	32.08%	
Equipment deposits prorated	<u>- 15,897</u>	<u>- 7,509</u>	<u>- 23,406</u>
Investment, as adjusted	<u>\$ 3,084,844</u>	<u>\$ 1,457,052</u>	<u>\$4,541,896</u>
Differentiated rates of return	5.50%	21.35%	
<u>Return on investment</u>	<u>\$ 169,666</u>	<u>\$ 311,081</u>	<u>\$ 480,747</u>
Return as percent of investment			10.58%
Tax, reflecting interest expense of \$200,289			292,371
Total return and tax			<u>\$ 773,118</u>
Subsidy requirement: breakeven need, return and tax			
Dollars			<u>\$6,306,277</u>
Per Available seat mile			<u>1.6402¢</u>

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LOCAL SERVICE CLASS SUBSIDY RATE

Ozark Air Lines, Inc.
Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Breakeven Need</u>
<u>Operating results, as reported 12- months 6/30/60</u>	\$7,757,823	\$11,735,763	\$3,977,940
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per passenger	670,256		- 670,256
Depreciation	- 68,000		- 68,000
Miscellaneous	- 16,000		- 16,000
Financing expenses	- 29,000		- 29,000
Entertainment expense	- 4,000		- 4,000
Amortization	- 1,000		- 1,000
<u>Operating results, as adjusted</u>	<u>\$8,428,079</u>	<u>\$11,617,763</u>	<u>\$3,189,684</u>
<u>Investment as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
<u>As reported June 30, 1960</u>	<u>\$2,279,937</u>	<u>\$ 872,429</u>	<u>\$3,152,366</u>
Transfer of 75% of notes payable to long-term debt	503,808		503,808
Unamortized discount and expense on debt	- 3,860		- 3,860
Estimated additional past period mail pay		- 462,000	<u>462,000</u>
Investments, as adjusted	<u>\$2,779,885</u>	<u>\$ 1,334,429</u>	<u>\$4,114,314</u>
Differentiated rates of return	<u>5.50%</u>	<u>21.35%</u>	
<u>Return on investment</u>	<u>\$ 152,894</u>	<u>\$ 284,901</u>	<u>\$ 437,795</u>
Return as percent of investment			10.64%
Tax, reflecting interest expense of \$106,609			347,327
Total return and tax			<u>\$ 785,122</u>
<u>Subsidy requirement: breakeven need, return and tax</u>			<u>\$3,974,806</u>
Dollars			<u>1.7829¢</u>
Per Available seat mile			

LOCAL SERVICE CLASS SUBSIDY RATE

Pacific Air Lines, Inc.
 Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Breakeven Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	\$7,329,070	\$10,875,640	\$3,546,570
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per passenger	565,564		- 565,564
Depreciation		- 14,000	- 14,000
Entertainment expenses		- 4,000	- 4,000
<u>Operating results, as adjusted</u>	<u>\$7,894,634</u>	<u>\$10,857,640</u>	<u>\$2,963,006</u>
<u>Investments as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported, June 30, 1960	\$4,512,383	\$ 903,562	\$5,415,945
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	770,569		770,569
Unamortized discount and expense on debt	- 11,157		- 11,157
Estimated additional past period mail pay		684,000	684,000
Sub-total	<u>\$5,271,795</u>	<u>\$ 1,587,562</u>	<u>\$6,859,357</u>
Debt-equity ratio	<u>76.86%</u>	<u>23.14%</u>	
Equipment deposits prorated	<u>- 62,880</u>	<u>- 18,931</u>	<u>- 81,811</u>
Investment, as adjusted	<u>\$5,208,915</u>	<u>\$ 1,568,631</u>	<u>\$6,777,546</u>
Differentiated rates of return	<u>5.50%</u>	<u>21.35%</u>	
<u>Return on investment</u>	<u>\$ 286,490</u>	<u>\$ 334,903</u>	<u>\$ 621,393</u>
Return as percent of investment			9.17%
Tax, reflecting interest expense of \$270,991			<u>368,144</u>
Total return and tax			<u>\$ 989,537</u>
Subsidy requirement: breakeven need, return and tax			
Dollars			<u>\$3,952,543</u>
Per Available seat mile			<u>1.7627¢</u>

LOCAL SERVICE CLASS SUBSIDY RATE

Piedmont Airlines
Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

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	<u>Revenues</u>	<u>Expenses</u>	<u>Breakeven Need</u>
Operating results, as reported 12-months 6/30/60	<u>\$7,919,164</u>	<u>\$12,008,885</u>	<u>\$4,089,721</u>
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per passenger	585,129	- 265,000	- 585,129
Depreciation	- 30,000	- 30,000	- 30,000
Accrued vacation expense	20,000	- 9,000	20,000
Out of period expenses	- 9,000	- 9,000	- 9,000
Entertainment expenses	- 9,000	- 9,000	- 9,000
Financing expenses	- 2,000	- 2,000	- 2,000
Bad Debts	- 1,000	- 1,000	- 1,000
Executive salaries	<u>\$8,504,293</u>	<u>\$11,712,885</u>	<u>\$3,208,592</u>
Operating results, as adjusted			
Investment as of June 30, 1960	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported, June 30, 1960	\$4,870,973	\$ 2,167,066	\$7,038,039
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	582,897		582,897
Unamortized discount and expense on debt	- 101,054		- 101,054
Estimated additional past period mail pay	338,217	338,217	
Accrued vacation liability	165,103	165,103	
Depreciation	387,724	387,724	
Bad debts	8,298	8,298	
Cash surrender value	- 13,600		
Separately operated division	-1,238,207		
Sub-total	<u>\$5,352,816</u>	<u>\$ 1,814,601</u>	<u>\$7,167,417</u>
Debt-equity ratio	74.68%	25.32%	
Adjustment Prorated:			
Separately operated division	- 345,674	- 117,200	- 462,874
Insurance premium fund deposit	- 66,714	- 22,619	- 89,333
Special deposit	- 7,468	- 2,532	- 10,000
Extension and development	- 1,491	- 505	- 1,996
	<u>- 421,347</u>	<u>- 142,856</u>	<u>- 564,203</u>
Investment as adjusted	<u>\$4,931,469</u>	<u>\$ 1,671,745</u>	<u>\$6,603,214</u>
Differentiated rates of return	5.50%	21.35%	
Return on investment	<u>\$ 271,231</u>	<u>\$ 356,918</u>	<u>\$ 628,149</u>
Return as percent of investment			9.51%
Tax, reflecting interest expense of \$327,637			314,096
Total return and tax			<u>\$ 942,245</u>
Subsidy requirement: breakeven need, plus return and tax			
Dollars		<u>\$4,150,837</u>	
Per Available seat mile		<u>1.8314¢</u>	

LOCAL SERVICE CLASS SUBSIDY RATE

Southern Airways, Inc.
 Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Break-even Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	\$3,770,276	\$6,868,416	\$3,098,140
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per passenger	319,026		- 319,026
Out of period expenses		- 77,000	- 77,000
Accrued vacation expense		- 39,000	- 39,000
Entertainment expense		- 19,000	- 19,000
Bad Debts		- 1,000	- 1,000
<u>Operating results, as adjusted</u>	<u>\$4,089,302</u>	<u>\$6,732,416</u>	<u>\$2,643,114</u>
<u>Investment as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
<u>As reported, June 30, 1960</u>	<u>\$ 105,000</u>	<u>\$ 746,382</u>	<u>\$ 851,382</u>
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	510,000		510,000
Estimated additional past period mail pay		711,000	711,000
Accrued vacation liability		181,438	181,438
Sub-total	<u>\$ 615,000</u>	<u>\$1,638,820</u>	<u>\$2,253,820</u>
Debt-equity ratio	<u>27.29%</u>	<u>72.71%</u>	
Adjustments Prorated:			
Equipment deposits	- 7,733	- 20,605	- 28,338
Investment as adjusted	<u>\$ 607,267</u>	<u>\$1,618,215</u>	<u>\$2,225,482</u>
Rate of return	<u>5.50%</u>	<u>21.35%</u>	
<u>Return on investment</u>	<u>\$ 33,400</u>	<u>\$ 345,489</u>	<u>\$ 378,889</u>
Return as percent of investment			17.03%
To provide maximum return of 12.75%			283,749
Tax reflecting \$29,652 interest expense			<u>263,813</u>
Total return and tax			<u>\$ 547,562</u>
Subsidy requirement: break-even need, return and tax			
Dollars			<u>\$3,190,676</u>
Per Available seat mile			<u>2.5256¢</u>

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LOCAL SERVICE CLASS SUBSIDY RATE

Trans-Texas Airways, Inc.
 Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Breakeven Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	\$5,486,965	\$8,375,134	\$2,888,169
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per psgr.	393,147		- 393,147
Accrued vacation expenses		- 18,000	- 18,000
Miscellaneous		- 8,000	- 8,000
Executive salaries		- 7,000	- 7,000
Out of period		- 2,000	- 2,000
<u>Operating results, as adjusted</u>	<u>\$5,880,112</u>	<u>\$8,340,134</u>	<u>\$2,460,022</u>
<u>Investment as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported, June 30, 1960	\$ 450,000	\$1,183,374	\$1,633,374
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	195,000		195,000
Accrued vacation liability		177,577	177,577
Sub-total	<u>\$ 645,000</u>	<u>\$1,360,951</u>	<u>\$2,005,951</u>
Debt-equity ratio	32.15%	67.85%	
Adjustments Prorated:			
Equipment deposits	- 16,319	- 34,440	- 50,759
Separately operated division	- 23,784	- 50,195	- 73,979
	<u>- 40,103</u>	<u>- 84,635</u>	<u>- 124,738</u>
<u>Investment, as adjusted</u>	<u>\$ 604,897</u>	<u>\$1,276,316</u>	<u>\$1,881,213</u>
Differentiated rates of return	5.50%	21.35%	
<u>Return on Investment</u>	<u>\$ 33,296</u>	<u>\$ 272,493</u>	<u>\$ 305,762</u>
Return as percent of investment			16.25%
To provide minimum return of 3¢ per mile			246,308
Tax, reflecting interest expense of \$43,083			<u>208,702</u>
Total return and tax			<u>\$ 455,010</u>
<u>Subsidy requirement: breakeven need, return and tax</u>			
Dollars			<u>\$2,915,032</u>
Per Available seat-mile			<u>1.4819¢</u>

LOCAL SERVICE CLASS SUBSIDY RATE

West Coast Airlines, Inc.
Calculation of Subsidy Requirement
Twelve Months Ended June 30, 1960

	<u>Revenues</u>	<u>Expenses</u>	<u>Break-even Need</u>
<u>Operating results, as reported 12-months 6/30/60</u>	\$5,990,861	\$10,954,991	\$4,964,130
Adjustments:			
Fare increase, 2 1/2% plus 90¢ per psgr.	483,286		- 483,286
Depreciation		- 198,000	- 198,000
Amortization		- 50,000	- 50,000
Overhaul accounting expense		- 30,000	- 30,000
Entertainment expense		- 6,000	- 6,000
Miscellaneous expenses		- 4,000	- 4,000
<u>Operating results, as adjusted</u>	<u>\$6,474,147</u>	<u>\$10,666,991</u>	<u>\$4,192,844</u>
<u>Investment as of June 30, 1960</u>	<u>Long-term Debt</u>	<u>Equity</u>	<u>Total</u>
As reported, June 30, 1960	\$3,942,776	\$ - 512,358	\$3,430,418
Adjustments Directly Assigned:			
Transfer of 75% of notes payable to long-term debt	738,275		738,275
Unamortized discount and expense on debt	- 37,418		- 37,418
Estimated additional past period mail pay		1,800,000	1,800,000
		91,169	91,169
Depreciation			84,311
Other	84,311		
Sub-total	<u>\$4,727,944</u>	<u>\$ 1,378,811</u>	<u>\$6,106,755</u>
Debt-equity ratio	<u>77.42%</u>	<u>22.58%</u>	
Adjustments Prorated:			
Equipment deposits	- 2,725	- 795	- 3,520
Investment, as adjusted	<u>\$4,725,219</u>	<u>\$ 1,378,016</u>	<u>\$6,103,235</u>
Rate of return	5.50%	21.35%	
<u>Return on investment</u>	<u>\$ 259,887</u>	<u>\$ 294,206</u>	<u>\$ 554,093</u>
Return as percent of investment			9.08%
Tax reflecting interest expense \$264,707			302,043
Total return and tax			<u>\$ 856,136</u>
Subsidy requirement: breakeven need, return and tax			
Dollars			<u>\$5,048,980</u>
Per available seat-mile			<u>2.4635¢</u>

LOCAL SERVICE CLASS SUBSIDY RATE

Revenue Plane Miles and Available Seat Miles
By Carrier and by Type of Aircraft
Twelve Months Ended June 30, 1960

	<u>Allegheny</u>	<u>Bonanza</u>	<u>Central</u>	<u>Frontier</u>	<u>Lake Central</u>	<u>Sohawk</u>	<u>North Central</u>	<u>Ozark</u>	<u>Pacific</u>	<u>Piedmont</u>	<u>Southern</u>	<u>Trans-Texas</u>	<u>West Coast</u>	<u>Total</u>
<u>Revenue Plane Miles</u>														
DC-3	2,719,957	1,943,596	4,010,479	7,931,641	3,688,677	1,501,915	11,885,273	8,264,464	1,203,096	3,922,988	5,263,847	8,196,354	3,533,150	64,065,437
CV-240							2,658,933							2,658,933
CV-340					1,655,444			2,255,376						3,910,820
JY-440		446,512					1,356,719							1,603,231
CV-540		495,398												495,398
M-202		3,662,337							1,832,077					5,494,414
4-404									554,358					554,358
P-27		2,648,426						614,890	2,441,924	3,012,408				3,003,831 12,021,472
Total	<u>7,324,204</u>	<u>4,592,022</u>	<u>4,010,479</u>	<u>9,587,085</u>	<u>3,688,677</u>	<u>5,517,567</u>	<u>14,140,649</u>	<u>8,879,354</u>	<u>6,031,455</u>	<u>7,235,396</u>	<u>5,263,647</u>	<u>8,196,354</u>	<u>6,536,381</u>	<u>31,304,372</u>
<u>Available Seat Miles (000)</u>														
DC-3	65,279	46,646	96,251	190,359	88,528	36,046	285,247	198,347	28,874	94,152	126,332	196,712	84,796	1,537,569
CV-240						106,357								106,357
CV-340				72,840			99,237							172,077
CV-440		19,647				59,696								79,343
CV-540		25,761												25,761
M-202		146,493							73,283					219,776
4-404									24,392					24,392
P-27		105,937						24,596	97,677	132,496				120,153 480,853
Total	<u>257,180</u>	<u>152,583</u>	<u>96,251</u>	<u>263,199</u>	<u>88,528</u>	<u>202,099</u>	<u>384,484</u>	<u>222,943</u>	<u>224,226</u>	<u>226,648</u>	<u>126,332</u>	<u>196,712</u>	<u>204,749</u>	<u>2,646,134</u>

^{1/} In scheduled service, exclusive of extra section trips. Source: Form 41 schedule T-3.

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LOCAL SERVICE CLASS SUBSIDY RATE

Subsidy Requirement per Available Seat Mile by Carrier
 In Relation to Revenue Plane Miles per Station per Day
Twelve Months Ended June 30, 1960

	<u>Revenue Plane Miles per Station per Day a/</u>	<u>Subsidy Requirement per Available Seat Mile b/</u>
Central	313	3.1345¢
Lake Central	348	1.8059
Frontier	383	2.7690
Southern	394	2.5256
West Coast	416	2.4635
Bonanza	502	2.3164
Ozark	546	1.7829
Trans Texas	554	1.4819
Piedmont	626	1.8314
North Central	646	1.6402
Pacific	649	1.7627
Allegheny	683	2.0514
Mohawk	739	1.5232

a/ Per Appendix A

b/ Per Appendix E

LOCAL SERVICE CLASS SUBSIDY RATE

Forecast Revenue Plane Miles and Available Seat Miles
By Carrier and by Type of Aircraft
Calendar Year 1961

	<u>Allegany</u>	<u>Bonanza</u>	<u>Central</u>	<u>Frontier</u>	<u>Lake Central</u>	<u>Hawk</u>	<u>North Central</u>	<u>Ozark</u>	<u>Pacific</u>	<u>Piedmont</u>	<u>Southern</u>	<u>Trans-Texas</u>	<u>West Coast</u>	<u>Total</u>	
Revenue Plane Miles															
DC-3	2,336,098		5,070,314	6,261,002	6,021,168	306,000	11,266,000	7,633,232	307,000	3,539,148	9,053,275	5,182,022	3,150,176	62,175,435	
CV-240			1,037,661			3,628,000						1,857,451		6,523,112	
CV-340				2,749,173	1,405,992		3,412,000							7,566,165	
CV-440	2,407,108					2,021,000								4,428,108	
CV-540	1,948,132													1,948,132	
M-202	3,827,282													3,827,282	
M-404							2,198,000							[69]	
P-27		4,371,348					1,285,377	2,915,000	3,572,357			3,627,728	15,571,810		
Total	10,518,620	4,371,348	6,107,975	9,009,175	7,427,160	6,455,000	14,673,000	8,913,609	5,920,000	7,161,505	9,053,275	8,039,473	6,777,304	104,338,044	69
Available Seat Miles (000)															
DC-3	56,066		121,688	150,264	114,508	19,344	270,384	183,193	19,368	36,140	217,279	148,369	75,604	1,492,212	
CV-240			41,506			145,120						74,298		260,924	
CV-340				120,920	61,864		150,128							332,912	
CV-440	105,913					88,924								194,837	
CV-540	101,303													101,303	
M-202	153,091													153,091	
M-404							96,712							96,712	
P-27		174,854					51,415	112,600	142,394					145,109	
Total	416,373	174,854	163,194	271,194	206,372	253,388	420,512	231,613	228,680	229,034	217,279	222,667	220,713	3,258,363	

Source: Carrier forecasts

LOCAL SERVICE CLASS SUBSIDY RATE

Rate per Available Seat Mile at Density Factors Ranging from
300 to 600 Revenue Plane Miles per Station per Day

Density Factor	Rate										
300 a/	3.1100¢	325	2.9600¢	350	2.8100¢	375	2.6600¢	400	2.5100¢	425	2.3600¢
301	3.1040	326	2.9540	351	2.8040	376	2.6540	401	2.5040	426	2.3540
302	3.0980	327	2.9480	352	2.7980	377	2.6480	402	2.4980	427	2.3480
303	3.0920	328	2.9420	353	2.7920	378	2.6420	403	2.4920	428	2.3420
304	3.0860	329	2.9360	354	2.7860	379	2.6360	404	2.4860	429	2.3360
305	3.0800	330	2.9300	355	2.7800	380	2.6300	405	2.4800	430	2.3300
306	3.0740	331	2.9240	356	2.7740	381	2.6240	406	2.4740	431	2.3240
307	3.0680	332	2.9180	357	2.7680	382	2.6180	407	2.4680	432	2.3180
308	3.0620	333	2.9120	358	2.7620	383	2.6120	408	2.4620	433	2.3120
309	3.0560	334	2.9060	359	2.7560	384	2.6060	409	2.4560	434	2.3060
310	3.0500	335	2.9000	360	2.7500	385	2.6000	410	2.4500	435	2.3000
311	3.0440	336	2.8940	361	2.7440	386	2.5940	411	2.4440	436	2.2940
312	3.0380	337	2.8880	362	2.7380	387	2.5880	412	2.4380	437	2.2880
313	3.0320	338	2.8820	363	2.7320	388	2.5820	413	2.4320	438	2.2820
314	3.0260	339	2.8760	364	2.7260	389	2.5760	414	2.4260	439	2.2760
315	3.0200	340	2.8700	365	2.7200	390	2.5700	415	2.4200	440	2.2700
316	3.0140	341	2.8640	366	2.7140	391	2.5640	416	2.4140	441	2.2640
317	3.0080	342	2.8580	367	2.7080	392	2.5580	417	2.4080	442	2.2580
318	3.0020	343	2.8520	368	2.7020	393	2.5520	418	2.4020	443	2.2520
319	2.9960	344	2.8460	369	2.6960	394	2.5460	419	2.3960	444	2.2460
320	2.9900	345	2.8400	370	2.6900	395	2.5400	420	2.3900	445	2.2400
321	2.9840	346	2.8340	371	2.6840	396	2.5340	421	2.3840	446	2.2340
322	2.9780	347	2.8280	372	2.6760	397	2.5280	422	2.3780	447	2.2280
323	2.9720	348	2.8220	373	2.6700	398	2.5220	423	2.3720	448	2.2220
324	2.9660	349	2.8160	374	2.6660	399	2.5160	424	2.3660	449	2.2160

a/ The rate of 3.1100¢ applies to density factors up to 300.

LOCAL SERVICE CLASS SUBSIDY RATE

Rate per Available Seat Mile at Density Factors Ranging from
300 to 600 Revenue Plane Miles per Station per Day

Density Factor	Rate	Density Factor	Rate	Density Factor	Rate	Density Factor	Rate	Density Factor	Rate	Density Factor	Rate
450	2.2100¢	475	2.1400¢	500	2.0700¢	525	2.000¢	550	1.9300¢	575	1.9150¢
451	2.2072	476	2.1372	501	2.0672	526	1.9972	551	1.9294	576	1.9144
452	2.2044	477	2.1344	502	2.0644	527	1.9944	552	1.9288	577	1.9138
453	2.2016	478	2.1316	503	2.0616	528	1.9916	553	1.9282	578	1.9132
454	2.1988	479	2.1288	504	2.0588	529	1.9888	554	1.9276	579	1.9126
455	2.1960	480	2.1260	505	2.0560	530	1.9860	555	1.9270	580	1.9120
456	2.1932	481	2.1232	506	2.0532	531	1.9832	556	1.9264	581	1.9114
457	2.1904	482	2.1204	507	2.0504	532	1.9804	557	1.9258	582	1.9108
458	2.1876	483	2.1176	508	2.0476	533	1.9776	558	1.9252	583	1.9102
459	2.1848	484	2.1148	509	2.0448	534	1.9748	559	1.9246	584	1.9096
460	2.1820	485	2.1120	510	2.0420	535	1.9720	560	1.9240	585	1.9090
461	2.1792	486	2.1092	511	2.0392	536	1.9692	561	1.9234	586	1.9084
462	2.1764	487	2.1064	512	2.0364	537	1.9664	562	1.9228	587	1.9078
463	2.1736	488	2.1036	513	2.0336	538	1.9636	563	1.9222	588	1.9072
464	2.1708	489	2.1008	514	2.0308	539	1.9608	564	1.9216	589	1.9066
465	2.1680	490	2.0980	515	2.0280	540	1.9580	565	1.9210	590	1.9060
466	2.1652	491	2.0952	516	2.0252	541	1.9552	566	1.9204	591	1.9054
467	2.1624	492	2.0924	517	2.0224	542	1.9524	567	1.9198	592	1.9048
468	2.1596	493	2.0896	518	2.0196	543	1.9496	568	1.9192	593	1.9042
469	2.1568	494	2.0868	519	2.0168	544	1.9468	569	1.9186	594	1.9036
470	2.1540	495	2.0840	520	2.0140	545	1.9440	570	1.9180	595	1.9030
471	2.1512	496	2.0812	521	2.0112	546	1.9412	571	1.9174	596	1.9024
472	2.1484	497	2.0784	522	2.0084	547	1.9384	572	1.9168	597	1.9018
473	2.1456	498	2.0756	523	2.0056	548	1.9356	573	1.9162	598	1.9012
474	2.1428	499	2.0728	524	2.0028	549	1.9328	574	1.9156	599	1.9006
									600 b/		1.9000

b/ The rate for density factors above 600 shall be computed by multiplying the rate of 1.9000¢ by the ratio of 600 to such density factors above 600.

Appendix J

LOCAL SERVICE CLASS SUBSIDY RATE
Subsidy Accruals
Fiscal Years 1951 through 1960

<u>Fiscal Year</u>	<u>Subsidy Amount (000)</u>	<u>Revenue Per Passenger Mile</u>	<u>Subsidy as % of Total Revenue</u>
1951	\$17,310	7.21¢	52.08%
1952	18,990	6.14	48.48
1953	21,850	5.89	47.01
1954	24,299	5.89	46.46
1955	22,568	4.52	39.35
1956	24,210	4.19	37.46
1957	28,741	4.20	37.30
1958	33,051	4.24	37.02
1959	37,131	4.15	34.78
1960	54,399	4.96	38.61

**LOCAL SERVICE CLASS SUBSIDY RATE
COMPARISONS OF SELECTED DATA
DOMESTIC TRUNK AND LOCAL SERVICE CARRIERS
12 Months ended June 30, 1960**

<u>Carrier</u>	Over-all Revenue Ton Miles (000)	Revenue Passenger Miles (000)	Revenue Passenger Originations (000)	Average Number of Revenue Passengers per Aircraft	Average Number of Available Seats per Aircraft	Daily Route Mile Turnover
Trunks, domestic operations						
American	741,483	6,215,476	8,235	50.0	73.2	51.4
Braniff	109,025	989,411	2,172	29.8	53.7	17.3
Capital	164,375	1,559,864	3,755	25.8	46.8	35.4
Continental	88,622	852,596	1,284	36.3	69.0	14.3
Delta	188,913	1,706,361	3,203	37.4	64.0	22.5
Eastern	456,790	4,344,379	8,126	34.0	66.1	48.1
National	116,161	1,075,188	1,691	40.3	73.7	24.8
Northeast	56,927	553,587	1,355	29.6	57.2	20.2
Northwest	165,156	1,421,591	1,892	40.7	72.8	20.6
TWA	510,205	4,639,027	5,161	50.9	75.2	35.8
United	576,396	4,807,615	7,042	44.2	67.0	47.8
Western	103,047	981,362	1,757	39.7	66.3	14.6
Total	3,277,100	29,146,457	45,673	40.5	66.8	32.0
Local Service						
Allegheny	11,471	110,990	602	15.1	32.7	12.6
Bonanza	6,019	60,211	244	13.1	31.6	6.6
Central	3,285	31,503	162	7.8	21.0	4.6
Frontier	9,454	85,304	330	8.9	24.5	5.1
Lake Central	3,862	37,302	238	10.1	25.2	6.6
Mohawk	10,883	107,760	544	19.2	40.0	11.0
North Central	17,462	165,128	945	11.6	27.2	10.4
Ozark	10,025	96,037	548	10.8	26.0	8.1
Pacific	10,125	102,434	452	16.9	33.6	10.0
Piedmont	9,756	96,111	452	13.1	29.4	10.5
Southern	4,921	46,581	260	8.8	26.0	6.2
Trans-Texas	7,637	70,721	302	8.6	23.0	7.5
West Coast	8,767	87,744	379	13.3	30.5	6.2
Total	113,667	1,097,826	5,458	12.0	28.3	7.7
High Trunk Carrier	741,483	6,215,476	8,235	50.9	75.2	51.4
Low Trunk Carrier	56,927	553,587	1,284	25.8	46.8	14.3
High Local Service Carrier	17,462	165,128	945	19.2	40.0	12.6
Low Local Service Carrier	3,285	31,503	162	7.8	21.0	4.6

Source: Carrier reports on CAB Form 41 and route mile record of OCAS.

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LOCAL SERVICE CLASS SUBSIDY RATE
COMPARISONS OF SELECTED DATA
DOMESTIC TRUNK AND LOCAL SERVICE CARRIERS
12 Months ended June 30, 1960

<u>Carrier</u>	Average Stage Length	Average Length of Passenger Journey	Revenue Passengers per Route Mile per Day	Investment (000)	Total Operating Revenues (000)	Total Operating Expenses (000)
<u>Trunks, domestic operations</u>						
American	395.7	754.8	2,421.3	\$ 349,435	\$ 409,642	\$ 384,781
Braniff	228.6	455.5	509.5	56,251	70,145	67,666
Capital	256.5	415.4	911.1	56,627	105,650	110,639
Continental	256.8	664.0	517.0	55,490	57,277	51,687
Delta	251.8	532.7	811.4	77,203	115,846	108,547
Eastern	244.7	534.6	1,635.7	231,979	269,918	272,234
National	264.7	635.8	994.6	67,281	66,128	71,798
Northeast	225.3	408.6	597.2	24,143	34,538	40,297
Northwest	371.8	751.4	800.9	68,535	88,564	85,003
TWA	443.1	898.9	1,772.7	130,318	280,571	271,760
United	373.8	682.7	2,019.2	295,981	313,684	314,472
Western	290.4	558.5	578.0	43,553	64,445	55,143
Total	307.7	638.1	1,261.2	\$1,456,796	\$1,876,408	\$1,834,027
<u>Local Service</u>						
Allegheny	91.5	185.4	190.1	\$ 4,758	\$ 12,613	\$ 13,103
Bonanza	125.6	246.8	86.9	5,390	7,297	7,196
Central	79.4	194.5	35.5	454	5,347	5,616
Frontier	98.7	258.5	45.3	3,039	14,658	13,601
Lake Central	70.8	156.7	66.5	880	4,764	4,724
Mohawk	100.7	198.1	210.9	5,599	10,885	11,480
North Central	83.5	174.7	121.1	3,425	20,455	20,368
Ozark	87.9	175.3	87.1	3,048	11,571	11,735
Pacific	97.3	226.6	169.9	5,961	9,700	10,875
Piedmont	85.3	212.6	137.7	7,154	11,681	12,008
Southern	87.2	179.2	54.4	1,078	6,291	6,868
Trans-Texas	92.5	234.2	64.5	1,777	8,401	8,375
West Coast	88.9	231.5	82.9	4,173	10,165	10,954
Total	90.0	201.1	92.3	\$ 46,736	\$ 133,828	\$ 136,903
High Trunk Carrier	443.1	898.9	2,421.3	\$ 349,435	\$ 409,642	\$ 384,781
Low Trunk Carrier	225.3	408.6	509.5	24,143	34,538	40,297
High Local Service Carrier	125.6	258.5	210.9	7,154	20,455	20,368
Low Local Service Carrier	70.8	156.7	35.5	454	4,764	4,724

Source: Carrier reports on CAB Form 41 and route mile record of OCAS.

[Served March 8, 1961]

Order No. E-16485

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D. C.
on the 7th day of March, 1961

- - - - -
In the Matter of the Local :
Service Class Subsidy Rate : Docket 12004
Investigation :
- - - - -

ORDER FIXING FINAL RATES

On February 16, 1961, the Board adopted Order E-16380, directing each of the parties herein to show cause why the Board should not adopt the findings and conclusions and fix, determine and publish the rates therein set forth as the fair and reasonable rates of compensation to be paid for the transportation of mail by aircraft for the period beginning January 1, 1961.

The time designated for filing notice of objection has elapsed and no notice of objection or answer to the order has been filed by Allegheny Airlines, Inc., Bonanza Air Lines, Inc., Lake Central Airlines, Inc., Mohawk Airlines, Inc., North Central Airlines, Inc., Ozark Air Lines, Inc., Piedmont Aviation, Southern Airways, Inc., or Trans Texas Airways.

The above-named parties have therefore waived the right to a hearing and all other procedural steps short of final decision of the Board fixing the rates.

The Board, upon consideration of the record hereby reaffirms and makes final all of the findings and conclusions set forth in the said order, except as specified below.

Upon a review of the class subsidy rate formula proposed in Order E-16380, the Board has concluded that certain changes of an editorial nature are desirable. These changes are as follows:

1. The definition of revenue plane miles in Section I A has been revised to clarify the provision regarding suspended route segments.
2. The references to "the requirements of the Act" in Sections III A (1) and III B (1) have been modified so as to refer only to reporting requirements.
3. The provision in Section III B (3) (a) regarding non-allowable expenses has been clarified.

4. The condition regarding payments to officers, directors, employees and stockholders in Section III B(3)(f) has been modified to reflect a more appropriate standard.
5. Clarifying language has been added to Section III B(3)(n) dealing with non-transport expenses.
6. The conditions regarding depreciation expenses have been made more precise. (Section III B(5)(a) and (b)).
7. The provision in Section III C(2)(h) concerning reserves has been limited to reserves other than valuation reserves.

Eight days will be provided for the filing of exceptions in the absence of which the rates set forth herein will become final automatically.

ACCORDINGLY, IT IS ORDERED, That the fair and reasonable rates of compensation on and after January 1, 1961, to be paid

Allegheny Airlines, Inc.
Bonanza Air Lines, Inc.
Lake Central Airlines, Inc.
Mohawk Airlines, Inc.
North Central Airlines, Inc.
Ozark Air Lines, Inc.
Piedmont Aviation, Inc.
Southern Airways, Inc.
Trans Texas Airways

for the transportation of mail by aircraft, the facilities used and useful therefor and the services connected therewith, between the points between which the carrier has been, is presently, or hereafter may be authorized to transport mail by its certificates of public convenience and necessity are the sum of (a) the service mail rates as heretofore and hereafter established for the carrier by Board orders pursuant to section 406(c) of the Act and (b) the subsidy rate for the carrier as set forth in the paragraphs below.

I. The subsidy rate for each carrier for each calendar month on and after January 1, 1961, shall be the rate per available seat mile determined in accordance with Appendix I (attached hereto) on the basis of the carrier's average number of revenue plane miles flown per station per day in the month; said subsidy rate to be applied to the available seat miles flown in the month, computed in accordance with the provisions and definitions set forth below.

A. The revenue plane miles flown shall be computed on the direct airport-to-airport mileage between the points actually served on each revenue trip operated over the carrier's routes pursuant to its flight schedules filed with the Board but exclusive of (1) trips flown as extra sections, (2) trips flown pursuant to authority of either certificates of public convenience and necessity or exemption orders issued pursuant

to section 416(b) of the Act which do not include authority to transport mail or which expressly include mail authority on a non-subsidy eligibility basis and (3) trips flown over route segments which the Board has, pursuant to Part 205 of the Economic Regulations, authorized the carrier to suspend for economic (as opposed to operational) reasons or the extra mileage involved in serving a point which the Board has authorized the carrier to suspend for economic (as opposed to operational) reasons.

B. The available seat miles flown each month (rounded to the nearest thousand) shall be the product of (1) the revenue plane miles flown computed in accordance with (A) above and (2) the standard number of seats for the respective aircraft types as follows:

<u>Aircraft Type</u>	<u>Standard Seats</u>
DC-3	24
CV-240; F-27; M-202	40
CV-340; CV-440; M-404	44
CV-540	52

C. The term "station" shall be deemed to be the monthly average number of airports operated for the carrier, computed on an airport-day basis, with each airport given weight proportional to the number of days operated during the month pursuant to Board authorizations; provided, however, that any airport serving a point which the Board has authorized the carrier to suspend for economic reasons shall not be included in the computation of airports operated. Airports served a full month shall be given a weight equal to the number of days in the month; airports served less than a full month shall be given a weight equal to the number of days service was authorized. The aggregate number of airport-days shall be divided by the appropriate number of days in the month to derive the weighted number of airports operated. The computation shall be carried out to one decimal place.

D. In computing the revenue plane miles flown per station per day for each month, the number of days in the month shall be based on the number of days in the calendar month exclusive of days on which operations are completely suspended due to a strike or similar work stoppage. On any days of partial reduction of operations due to strikes or similar work stoppage, when the revenue plane miles flown by the carriers are less than 90 percent

of the revenue plane miles scheduled to be flown for such days, such days shall be counted as a reduced number of days to be arrived at by multiplying the number of such days by the ratio of (1) the revenue plane miles flown on such days divided by (2) the product of the revenue plane miles scheduled to be flown on such days ^{1/} times

^{1/} Based on the carrier's official schedules on file with the Board on the last day prior to the work stoppage.

the system average performance factor of the carrier during the corresponding month or months of the prior year.

E. The subsidy otherwise payable to the carrier under this Section (I) above shall be reduced by the amount of any adjusted annual capital gain in accordance with the provisions set forth in Appendix B to Order E-14104, dated June 24, 1959, as such Appendix B may be amended from time to time, and said Appendix B is hereby incorporated herein by reference.

F. The subsidy otherwise payable to the carrier under this Section (I) above shall be subject to reduction in accordance with the Profit Sharing terms and conditions specified in (II) below.

II. The annual subsidy otherwise due and payable to each carrier pursuant to (I) above, shall be subject to reduction to the extent that the carrier's earnings for calendar year 1961 and each succeeding calendar year exceed the carrier's fair and reasonable differentiated rate of return, in accordance with the provisions set forth below. In the event that this class rate terminates prior to the last day of a calendar year and is not superseded by a class rate containing profit-sharing provisions, the subsidy otherwise due and payable to each carrier pursuant to Section I for any such period of less than a calendar year shall be subject to re-

duction in like manner, provided that the results of the carrier for such period shall be adjusted to eliminate seasonal distortions.

A. Each carrier's fair and reasonable differentiated rate of return shall be the weighted average rate of return arrived at by applying rates of 21.35%, 7.5% and 5.5% to the common stock equity, preferred stock equity and debt components of recognized investment, respectively; provided that (1) the maximum rate of return computed in accordance with the preceding portion of this paragraph shall not exceed 12.75% (after applicable income taxes) and shall not be less than 9.00% (after applicable income taxes), and (2) in no event shall the fair and reasonable differentiated rate of return be less than the equivalent of three cents (after applicable income taxes) per revenue plane mile flown (in accordance with the definition of revenue plane miles flown as defined in IA, above).

B. In any case where a carrier's annual earnings (after applicable income taxes) exceed its fair and reasonable differentiated rate of return, such carrier shall refund a portion of such profits to the extent

indicated in the Table below to the Board as subsidy not due the carrier:

<u>Rate of Return (After Taxes)</u>	<u>Percentage of Profits Refunded by Carrier</u>
0% to D ^{2/}	0%
D to 15%	50%
Over 15%	75%

C. In applying the Table in B above, the amounts due to be refunded to the Board in any calendar year shall be reduced by the amount of any earnings deficiency of the carrier in the two preceding calendar years (exclusive of periods prior to January 1,

1961). An earnings deficiency is defined as the amount by which the carrier's earnings (after applicable income taxes) in a calendar year are less than the fair and reasonable differentiated rate of return specified in IIA above.

III. In applying the provisions of II, above, the revenues and other income items, expenses, investment and income taxes shall be determined in accordance with the provisions of this Section III.

A. Revenues

1. The revenues shall be those reported by each carrier on its Form 41 reports to the Board, provided that such reports are consistent with the reporting requirements of the Act and the Board's Regulations (particularly Part 241 and the Uniform System of Accounts for Air Carriers) and that such reports reflect accounting practices consistent with the carrier's practices in reports for prior periods, except in cases where the carrier has obtained Board approval for change in such accounting practices.

2. The revenues in reports not complying with 1, above, shall be adjusted to comply therewith in applying the provisions of II, above.

3. Revenues reported from non-transport activities or from transactions with affiliates shall be excluded unless the profit (after income taxes) to the carrier from such activities exceeds the fair and reasonable differentiated rate of return for the carrier for air transport operations, in which case such excess shall be utilized for the purpose of II, above. For the purpose of this entire Section III, the term affiliate (or affiliated) shall be deemed to include any

2/ D represents the fair and reasonable differentiated rate of return for each carrier as defined in IIA, above.

"associated company" as defined at page 31.2 of the Uniform System of Accounts or any relationship defined as "affiliated" in Part 261.8(b) of the Board's Economic Regulations, as amended.

B. Operating Expenses

1. The operating expenses shall be those reported by each carrier on its Form 41 reports to the Board provided that such reports are consistent with the reporting requirements of the Act and the Board's Regulations (particularly Part 241 thereof and the Uniform System of Accounts) and that such reports reflect accounting practices consistent with the carrier's accounting in previous periods, except in cases where the carrier has obtained Board approval for change in such accounting practice, and pro-
vided further that reporting and accounts not complying with this paragraph 1 shall be adjusted to comply therewith in applying the provisions of II, above.

2. The operating expenses otherwise reported or determined in accordance with paragraph 1, above, shall be subject to the conditions set forth below.

3. Non-allowable expenses - The following operating expense items shall not be recognized and shall be disallowed:

- a. Any reported expense prohibited by the Act, or any other provisions of law, or regulation of the Board or other agency of Government;
- b. Fines or other similar penalties accrued, or paid, as the result of violation of law or in violation of any association rule or by-law;
- c. All financing costs and costs related to financing;
- d. Lobbying costs;
- e. Compensation, in any form whatsoever, paid directly or indirectly to or on behalf of any officer, director, or employee, of the carrier in excess of \$25,000 per annum;

f. Any payment made directly or indirectly, in any form whatsoever, to or on behalf of any officer, director or employee of the carrier, or to or on behalf of any stockholder owning in excess of a 1 percent stock interest, to the extent that such payment exceeds the reasonable value of the goods or services received;

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g. Any payment to directors, officers or employees in the nature of bonuses related to profits or representing a sharing of profits;

h. Any form of dues (including initiation fees) expensed on behalf of the carrier or any officer or director, unless such dues are for membership in a business, professional or trade organization;

i. Any self-insurance or other accruals requiring Board approval of the basis of accrual, unless approved by the Board or by the Board's staff under delegated authority;

j. Expenses incurred and accrued for proceedings in which the carrier is an unsuccessful applicant for an exemption or route award, or is an intervenor; Provided further that during its prosecution of an exemption or route award expenses incurred by the carrier for that purpose shall be held in suspense, for the purpose of this order, pending final decision of the Board, and if the carrier receives an award thereunder the expenses related to the carrier's successful prosecution of its case shall be recognized by amortization over a period of 5 years or the period of the award, if shorter, such amortization to commence as of the date of institution of the service provided pursuant to the Board's final decision in the exemption or route proceedings; 3/

k. Expenses in proceedings before the Board for witnesses other than the carrier's personnel or consultants hired by the carrier;

l. Contributions on behalf of the carrier for charitable or similar purposes;

m. Premiums for life insurance on the life of any officer, director or employee where the company is a named beneficiary;

n. Expenses incurred in non-transport activities and any other expense which is not reasonably related to the air transport services of the carrier, except to the extent that such expenses are offset against revenues from such activities in accordance with III A 3 above.

3/ In cases covered by this proviso clause where the Board prior to January 1, 1961, has established a final subsidy rate which would otherwise be applicable on and after January 1, 1961, amortization shall be recognized as per such final rate order.

4. The following expenses shall be recognized to the extent indicated:

a. Expenses incurred by the carrier in dealings with an affiliate (including a separately operated division) shall be recognized only to the extent that the charges by the affiliate are at cost, including a proper share of overhead and a capital cost not exceeding the level of the air carrier's own fair and reasonable differentiated rate of return;

b. Costs which result from transactions not at arms length, dealings involving conflicts of interest, or involving fraud on the part of the air carrier, its personnel

or any person under the carrier's control shall be recognized only to the extent that such costs do not exceed reasonable levels;

c. In case the carrier enters into a sale of equipment, with a provision for lease-back of such equipment or similar equipment, any cost exceeding that which would have been incurred had such sale and lease-back not occurred will not be recognized.

5. The depreciation expense to be recognized for flight equipment (including hulls and all related flight components) shall be subject to the following additional special rules and conditions:

a. For flight equipment acquired and placed into service prior to January 1, 1961, the recognizable expense shall be based on the book value recorded as of December 31, 1960, plus any betterment or improvements subsequent to that date, provided that such value does not exceed the depreciated original cost including betterments or improvements, of such equipment to the air carrier;

b. For flight equipment acquired and placed into service on or after January 1, 1961, the recognizable expense shall be based on the depreciable original cost of such equipment (including betterments or improvements and capitalized interest) to the air carrier;

c. The service lives and residual values for flight equipment (including hulls and all related components) shall be as set forth in the following table;

<u>Equipment type</u>	<u>Service life</u>	<u>Residual value</u>
DC-3	3 years	10%
all other piston-powered aircraft	7 years	15%
turbine-powered aircraft	10 years	15%

d. The service life for each aircraft type shall be deemed to commence as of the date of its introduction into regularly scheduled service, provided that the remaining service life for aircraft placed into service prior to January 1, 1961, shall be computed by subtracting from the years of service life set out in the table above the periods prior to January 1, 1961, for which depreciation has been accrued by the air carrier for such flight equipment, and the remainder of the depreciable value so derived shall be spread out equally each month from January 1, 1961 forward; ^{4/}

e. For the purpose of this paragraph 5, the otherwise recognizable depreciable cost for aircraft hulls and engines shall be reduced by the value of the so-called "built-in-overhaul," such value to be determined at a reasonable level consistent with prior and anticipated experience; Provided, however, that where aircraft are maintained on a phase or pattern overhaul basis, the depreciable cost shall be reduced by only 50 percent of the value of the "built-in-overhaul" plus the value of the hours remaining to the next phase or pattern overhaul; Provided further that maintenance charges will be recognized consistent with the built-in-overhaul principle, and that accruals to a reserve for future overhauls will not be recognized.

C. Investment

i. Subject to the same requirements as to compliance with the Act and the Board's Regulations, as set forth in A and B, above, the investment shall be the average of the balance sheets reported for the four quarters of the calendar year, for which Section II, above, is being applied, and the year end balance sheet for the immediately preceding year, with one-half weight accorded the opening and closing balance sheets.

2. The investment shall be subject to the additional special rules and conditions set forth below:

- a. Notes payable due beyond 90-days shall be treated as long-term debt;
- b. Non-operating property shall be excluded;

4/ Where a final rate has been established for the carrier prior to January 1, 1961, the "remaining service life" shall be based on the depreciation rates recognized in such final order (or orders).

c. The air carrier's investment in any affiliated or non-transport activity shall be recognized only in the event that the profits (after income taxes) reported by the air carrier from such company or activity exceed the fair and reasonable differentiated return of the air carrier and such profits are utilized to reduce the air carrier's subsidy;

d. The investment shall not include the cash or other value of any life insurance policy covering any company executive;

e. The investment shall not include equipment replacement funds derived from sale of flight equipment, but such funds shall be recognized only when re-invested in property which is productive in the carrier's transport operations;

f. The investment shall not include equipment purchase deposits, capitalized organizational expense, capital stock expense, unamortized discount and expense on debt, and/or special funds such as sinking funds as specified in Account 1550 in the Uniform Manual of Accounts;

g. Working capital in excess of the equivalent of 3 months' operating expenses, exclusive of depreciation and amortization, shall be excluded;

h. Reserves accrued through charges to operating expense (except depreciation, airworthiness and other valuation reserves) will be treated as a current liability for the purpose of this paragraph C;

i. Construction work in progress shall be recognized only to the extent that capitalized interest on such item is not claimed by the carrier;

j. The computation of working capital related to periods prior to January 1, 1961, shall reflect the subsidy payable to the air carrier pursuant to the most recent Board order dealing with the carrier's subsidy for such period, but for periods commencing January 1, 1961, accruals for each balance sheet date shall be made pursuant to the rate established by this Order.

D. Other Income and Non-operating Expenses - In applying Section II, above, all income to the carrier (other than capital gains on flight equipment qualifying pursuant to Section 406(d) of the Act and the Board's Regulations thereunder) shall be included whether such income is recorded as revenue, non-operating income and/or Special Income; but only the following classes of non-operating expenses shall be recognized:

1. Capital losses on ground equipment; and
2. Non-routine foreign exchange adjustments.

E. Where an adjustment is required and effected pursuant to the provisions of paragraph III A or B or C or D above, such appropriate adjustments shall be made for the purpose of all other provisions of this Section III where sound accounting practice and consistency so require.

F. Income Taxes - Federal and State income taxes shall be determined on the basis of the carrier's income tax returns for

each year as submitted to the taxing authorities, with such amendments or revisions (including tax carry-back and carry forward credits) as may have been filed as of the date of the final determination of excess profits (or an earnings deficiency) under this Order, Provided, however, that for carriers whose tax returns are filed for a 12 month period not coinciding with a calendar year, a pro forma tax return will be required to be submitted for the calendar year, which return shall be prepared on bases consistent with the returns of that carrier filed for the latest fiscal year with the appropriate tax authorities. ^{5/}

G. The refund otherwise due and payable to the Government pursuant to Section II shall be increased by the amount of the income tax savings estimated to accrue to the carrier as the result of such refund.

IT IS FURTHER ORDERED, That the compensation provided herein shall be in lieu of, and not in addition to, the mail compensation heretofore received by the carriers named above for mail transported over their entire systems on and after January 1, 1961.

IT IS FURTHER ORDERED, That this order shall become effective on the eighth day after the date of service unless prior to that date exceptions (with respect to the changes described on pp. 1 & 2 hereof) and supporting reasons have been filed with the Board by any party named above. If exceptions and supporting reasons are filed within the prescribed time, the effective date of this order shall be stayed pending disposition of the exceptions.

By the Civil Aeronautics Board:

/s/ Robert C. Lester
Robert C. Lester
Secretary

(SEAL)

5/ A reconciliation of such pro forma return with the carrier's reported operating results will be required.

LOCAL SERVICE CLASS SUBSIDY RATE

Rate per Available Seat Mile at Density Factors Ranging from
300 to 600 Revenue Plane Miles per Station per Day

Density Factor	Rate										
300 a/	3.1100¢	325	2.9600¢	350	2.8100¢	375	2.6600¢	400	2.5100¢	425	2.3600¢
301	3.1040	326	2.9540	351	2.8040	376	2.6540	401	2.5040	426	2.3540
302	3.0980	327	2.9480	352	2.7980	377	2.6480	402	2.4980	427	2.3480
303	3.0920	328	2.9420	353	2.7920	378	2.6420	403	2.4920	428	2.3420
304	3.0860	329	2.9360	354	2.7860	379	2.6360	404	2.4860	429	2.3360
305	3.0800	330	2.9300	355	2.7800	380	2.6300	405	2.4800	430	2.3300
306	3.0740	331	2.9240	356	2.7740	381	2.6240	406	2.4740	431	2.3240
307	3.0680	332	2.9180	357	2.7680	382	2.6180	407	2.4680	432	2.3180
308	3.0620	333	2.9120	358	2.7620	383	2.6120	408	2.4620	433	2.3120
309	3.0560	334	2.9060	359	2.7560	384	2.6060	409	2.4560	434	2.3060
310	3.0500	335	2.9000	360	2.7500	385	2.6000	410	2.4500	435	2.3000
311	3.0440	336	2.8940	361	2.7440	386	2.5940	411	2.4440	436	2.2940
312	3.0380	337	2.8880	362	2.7380	387	2.5880	412	2.4380	437	2.2880
313	3.0320	338	2.8820	363	2.7320	388	2.5820	413	2.4320	438	2.2820
314	3.0260	339	2.8760	364	2.7260	389	2.5760	414	2.4260	439	2.2760
315	3.0200	340	2.8700	365	2.7200	390	2.5700	415	2.4200	440	2.2700
316	3.0140	341	2.8640	366	2.7140	391	2.5640	416	2.4140	441	2.2640
317	3.0080	342	2.8580	367	2.7080	392	2.5580	417	2.4080	442	2.2580
318	3.0020	343	2.8520	368	2.7020	393	2.5520	418	2.4020	443	2.2520
319	2.9960	344	2.8460	369	2.6960	394	2.5460	419	2.3960	444	2.2460
320	2.9900	345	2.8400	370	2.6900	395	2.5400	420	2.3900	445	2.2400
321	2.9840	346	2.8340	371	2.6840	396	2.5340	421	2.3840	446	2.2340
322	2.9780	347	2.8280	372	2.6760	397	2.5280	422	2.3780	447	2.2280
323	2.9720	348	2.8220	373	2.6700	398	2.5220	423	2.3720	448	2.2220
324	2.9660	349	2.8160	374	2.6660	399	2.5160	424	2.3660	449	2.2160

a/ The rate of 3.1100¢ applies to density factors up to 300.

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LOCAL SERVICE CLASS SUBSIDY RATE

Rate per Available Seat Mile at Density Factors Ranging from
300 to 600 Revenue Plane Miles per Station per Day

Density Factor	Rate	Density Factor	Rate	Density Factor	Rate	Density Factor	Rate	Density Factor	Rate	Density Factor	Rate
450	2.2100¢	475	2.1400¢	500	2.0700¢	525	2.000¢	550	1.9300¢	575	1.9150¢
451	2.2072	476	2.1372	501	2.0672	526	1.9972	551	1.9294	576	1.9144
452	2.2044	477	2.1344	502	2.0644	527	1.9944	552	1.9288	577	1.9138
453	2.2016	478	2.1316	503	2.0616	528	1.9916	553	1.9282	578	1.9132
454	2.1988	479	2.1288	504	2.0588	529	1.9888	554	1.9276	579	1.9126
455	2.1960	480	2.1260	505	2.0560	530	1.9860	555	1.9270	580	1.9120
456	2.1932	481	2.1232	506	2.0532	531	1.9832	556	1.9264	581	1.9114
457	2.1904	482	2.1204	507	2.0504	532	1.9804	557	1.9258	582	1.9108
458	2.1876	483	2.1176	508	2.0476	533	1.9776	558	1.9252	583	1.9102
459	2.1848	484	2.1148	509	2.0448	534	1.9748	559	1.9246	584	1.9096
460	2.1820	485	2.1120	510	2.0420	535	1.9720	560	1.9240	585	1.9090
461	2.1792	486	2.1092	511	2.0392	536	1.9692	561	1.9234	586	1.9084
462	2.1764	487	2.1064	512	2.0364	537	1.9664	562	1.9228	587	1.9078
463	2.1736	488	2.1036	513	2.0336	538	1.9636	563	1.9222	588	1.9072
464	2.1708	489	2.1008	514	2.0308	539	1.9608	564	1.9216	589	1.9066
465	2.1680	490	2.0980	515	2.0280	540	1.9580	565	1.9210	590	1.9060
466	2.1652	491	2.0952	516	2.0252	541	1.9552	566	1.9204	591	1.9054
467	2.1624	492	2.0924	517	2.0224	542	1.9524	567	1.9198	592	1.9048
468	2.1596	493	2.0896	518	2.0196	543	1.9496	568	1.9192	593	1.9042
469	2.1568	494	2.0868	519	2.0168	544	1.9468	569	1.9186	594	1.9036
470	2.1540	495	2.0840	520	2.0140	545	1.9440	570	1.9180	595	1.9030
471	2.1512	496	2.0812	521	2.0112	546	1.9412	571	1.9174	596	1.9024
472	2.1484	497	2.0784	522	2.0084	547	1.9384	572	1.9168	597	1.9018
473	2.1456	498	2.0756	523	2.0056	548	1.9356	573	1.9162	598	1.9012
474	2.1428	499	2.0728	524	2.0028	549	1.9328	574	1.9156	599	1.9006
									600 b/		1.9000

b/ The rate for density factors above 600 shall be computed by multiplying the rate of 1.9000¢ by the ratio of 600 to such density factors above 600.

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[Served May 24, 1961]

Order No. E-16842

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D. C.
on the 23rd day of May, 1961

- - - - -
In the Matter of the Local : Docket No. 12004
Service Class Subsidy Rate :
Investigation :
- - - - -

ORDER

On March 7, 1961, the Board, by order E-16485, established a local service carrier class subsidy rate. ^{1/} It was the clear intent of that order that subsidy not be paid for trips flown over route segments over which the Board has authorized the carriers to suspend service, and for other services not eligible for subsidy. ^{2/} However, the Board's attention has been drawn to the fact that there is an inadvertent ambiguity in the rate formula in that paragraph I C of the formula defining the term "station," is capable of being construed so as to permit suspended points and segments not eligible for subsidy to affect the calculation of the subsidy under the formula.

In order to clarify paragraph I C of the formula and to comply with the intent of the order, the language of that paragraph should be modified to remove any possible ambiguity in this regard.

ACCORDINGLY, IT IS ORDERED, That pursuant to the Federal Aviation Act of 1958, as amended, and particularly Section 406 thereof, paragraph I C of Order E-16485 be, and it hereby is, amended in its entirety to read as follows:

"C. The term "station" shall be deemed to be the monthly average number of airports operated for the carrier, computed on an airport-day basis, with each airport given weight proportional to the number of days operated

1/ This order applied to nine of the thirteen local carriers. It was extended to two additional carriers by Order E-16542, March 22, 1961.

2/ Order E-16485, page 2, paragraph I A.

during the month pursuant to Board authorizations; provided, however, that any airport serving a point exclusively on trips flown on non-mail or non-subsidy routes as per A (2) above, or any airport serving a point which the Board has authorized the carrier to suspend for economic reasons as per A (3) above, shall not be included in the computation of airports operated. Airports served a full month shall be given a weight equal to the number of days in the month; airports served less than a full month shall be given a weight equal to the number of days service was authorized. The aggregate number of airport-days shall be divided by the appropriate number of days in the month to derive the weighted number of airports operated. The computation shall be carried out to one decimal place."

IT IS FURTHER ORDERED, That the foregoing clarifying amendment, which does not affect the substance of the class rate order, shall be effective as of the date of the class rate, namely January 1, 1961.

IT IS FURTHER ORDERED, That this order shall become effective on the 11th day following its issuance, unless prior to that date exceptions and supporting reasons are filed by any of the eleven local service air carriers for whom the class rate was finalized by Orders E-16485 and E-16542. If exceptions are filed, this order shall be stayed pending disposition of such exceptions.

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IT IS FURTHER ORDERED, That this order be served upon each of the eleven local service carriers referred to in the preceding paragraph.

By the Civil Aeronautics Board.

/s/ Mabel McCart

Mabel McCart
Acting Secretary

(SEAL)

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[98]

NORTH CENTRAL AIRLINES, INC.

General Offices: 6201 Thirty-Fourth Avenue So.
Minneapolis 50, Minn.

March 22, 1963

Mr. Jack Herman, Chief
Carrier Payments Section
Civil Aeronautics Board
Washington, D. C.

Dear Jack:

Enclosed are our Profit Sharing Returns for 1962 together with
photostats of our Corporation Income Tax Returns.

If you desire any further information, please let me hear from
you.

Very truly yours,
NORTH CENTRAL AIRLINES, INC.

/s/ Daniel F. May
Assistant Treasurer

DFM/jd

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CAB Form T-88
(11-61)

CLASS RATE PROFIT SHARING SCHEDULE
PROFIT SHARING COMPUTATION
Carrier NORTH CENTRAL AIRLINES, INC. Year ended December 31, 1962

	Step I	Step II	Step III	Step IV	Step V
1. Income after tax, before profit sharing, per Schedule B	1,074,422	1,074.422	1,074.422	1,074,422	
2. Percent of investment $(1 + 8)$	14.34%	14.47%	14.48%	14.48%	
<u>Investment</u>					
3. Debt (Schedule W)	4,954,012	4,954,012	4,954.012	4,954,012	
4. Preferred equity (Schedule W)	2,536,627	2,536,627	2,536,627	2,536,627	
5. Common equity (Schedule W)		65,095	68,569	68,755	
6. Adjustment to common equity (50% of line 29)	2,536,627	2,471,532	2,468,058	2,467,872	
7. Common equity adjusted	7,490,639	7,425,544	7,422,070	7,421,884	
8. Total investment					
<u>Return Element</u>					
9. Debt $(5.50\% \times \text{Line 3})$	272,471	272,471	272,471	272,471	
10. Preferred equity $(7.50\% \times \text{Line 4})$	541,570	527,672	526,930	526,891	
11. Common equity $(21.35\% \times \text{Line 7})$	814,041	800,143	799,401	799,362	
12. Return element	10.87%	10.78%	10.77%	10.77%	
13. Percent of investment $(12 + 8)$					
14. Return at 12.75 percent					
15. Return at 9.00 percent					
16. Return at 3¢ per mile					
17. "D" return element *	814,041	800,143	799,401		
18. Earnings deficiency $(1 - 17)$					
<u>Profit Sharing</u>					
19. Profit to "D"	814,041	800,143	799,401		
20. "D" to 15 percent	260,381	274,279	275,021		
21. Over 15 percent					
22. Total	1,074,422	1,074,422	1,074,422		
<u>Carrier Share</u>					
23. Profit to "D" $(100\% \times \text{Line 19})$	814,041	800,143	799,401		
24. "D" to 15% $(50\% \times \text{Line 20})$	130,191	137,140	137,511		
25. Over 15% $(25\% \times \text{Line 21})$					
26. Net profit to carrier	944,232	937,283	936,912		
<u>Government's Share</u>					
27. "D" to 15% $(50\% \times \text{Line 20})$	130,190	137,139	137,510		
28. Over 15% $(75\% \times \text{Line 21})$	130,190	137,139	137,510		
29. Government share after tax					
30. Tax reduction	162,372	171,039	171,501		
31. Total profit sharing (Line 29 + 44.5)	292,562	308,178	309,011		

* Higher of 12, 15 or 16, provided that the computed return (Line 12) does not exceed an amount equivalent to 12.75 percent of recognized investment.

SCHEDULE A

CAR Form T-748
(11-61)CLASS RATE PROFIT SHARING SCHEDULE
SUMMARY INCOME STATEMENTCarrier NORTH CENTRAL AIRLINES, INC.Year ended December 31, 1962

1. Reported operating profit or loss, per Form 41			1,490,710
2. Adjustment for subsidy revenue			
a) Formula subsidy	8,841,757		
b) Reported per Form 41	8,526,611	315,146	
3. Adjustments per Schedule C			89,003
4. Nonoperating income per Schedule Q			14,141
5. Special income per Form 41			
<u>Adjustments:</u>			
a) Retroactive subsidy			
b) Special income debits			
c) Special income credits-other			
6. Adjusted income before income taxes			1,909,000
7. Adjusted income taxes per Schedule R			834,578
8. Adjusted net income after taxes, before profit sharing			1,074,422

SCHEDULE B

[101]

CAB Form T-88
(11-61)CLASS RATE PROFIT SHARING SCHEDULE
OPERATING REVENUES AND EXPENSES ADJUSTMENTSCarrier NORTH CENTRAL AIRLINES, INC.Year ended December 31, 1962

<u>Reference</u>	<u>Revenues</u>	
III A 1	1. Inconsistent reporting	None
III A 3	2. Nontransport or affiliate (See Schedule D)	None
	Total	None
<u>Expenses</u>		
VII B 1	1. Inconsistent reporting	None
III B 3a	2. Prohibited expenses	None
III B 3b	3. Fines, etc.	(1,879)
III B 3c	4. Financing costs	None
III B 3d	5. Lobbying costs	None
III B 3e	6. Compensation over \$25,000.	27,212
III B 3f	7. Payments in excess of goods or services	None
III B 3g	8. Bonuses	None
III B 3h	9. Nonallowable dues	None
III B 3i	10. Nonallowable accruals	44,118
III B 3j	11. Amortization of E & D (Details in Schedule V-1)	None
III B 3k	12. Witness fees	(656)
III B 3l	13. Charitable contributions	None
III B 3m	14. Life insurance premiums	(317)
III B 3n	15.a. Nontransport or affiliate expense (See Schedule D)	None
III B 3n	b. Expense not reasonably related to air service	None
III B 4a	16. Affiliate expenses in excess of cost	None
III B 4b	17. Unreasonable non-arm's length, etc., expenses	None
III B 4c	18. Sale and lease-back	17,673
III B 5	19. Depreciation in excess of allowable (Details in Schedule E)	None
III B 5e	20. Maintenance to conform to built-in overhaul (Details in Schedule E)	
	Total	89,003
	Net Adjustment	

SCHEDULE C

CAB Form T-38
(11-61)

CLASS RATE PROFIT SHARING SCHEDULE

NONTRANSPORT AND AFFILIATE ACTIVITIES

Carrier NORTH CENTRAL AIRLINES, INC.Year ended December 31, 1962

(Separate schedule is to be filled out for each activity)

(1) Gross revenues *	None
(2) Gross expenses *	None
(3) Net profit or loss* (-) before taxes /Account **	
(4) Applicable taxes per schedule S	
(5) Net profit or loss (-) after taxes	
(6) Investment in non-transport or affiliate activities	
(7) "E" rate of return	None
(8) "D" return	

Adjustments required (other than accounting):

A - If line (5) exceeds line (8) no adjustment is required to the reported results.

B - If line (5) is less than line (8)

(a) Delete reported net profit or loss before taxes (line 3 above) from Account 8186 of adjusted nonoperating income and expense-net in Schedule Q.

(b) Delete applicable taxes (line 4 above) from actual taxes in computing adjusted taxes in Schedule R.

(c) Eliminate investment (line 6 above) from Airline investment on Schedule W.

* Revenues and expenses are to be adjusted, if necessary, to correct accounting misclassification.
See Schedule C: Operating Revenue, Line 2; and Operating Expenses Line 15a.

** See Schedule Q.

SCHEDULE D

[103]

[103]

CAB Form T-88
(11-61)CLASS RATE PROFIT SHARING SCHEDULE
SUMMARY FLIGHT EQUIPMENT DEPRECIATION ADJUSTMENT BY QUARTERSCarrier NORTH CENTRAL AIRLINES, INC.Year ended December 31, 1962

	1st.Quarter	2nd.Quarter	3rd.Quarter	4th.Quarter	Year-to-date 1962
<u>Reported depreciation expense</u>					
Account No. 1601	23,295	21,361	19,659	17,866	82,181
" 1602					
" 1603					
" 1604					
" 1606					
" 1607					
" 1608					
Total flight equipment	23,295	21,361	19,659	17,866	82,181
<u>Computed depreciation expense</u>					
Account No. 1601	18,162	16,530	15,475	14,341	64,508
" 1602					
" 1603					
" 1604					
" 1606					
" 1607					
" 1608					
Total flight equipment.....	18,162	16,530	15,475	14,341	64,508
<u>Adjustment</u>					
Account No. 1601	5,133	4,831	4,184	3,525	17,673
" 1602					
" 1603					
" 1604					
" 1606					
" 1607					
" 1608					
Total flight equipment	5,133	4,831	4,184	3,525	17,673

SCHEDULE E

CLASS RATE PROFIT SHARING SCHEDULE
FLIGHT EQUIPMENT DEPRECIATIONCarrier NORTH CENTRAL AIRLINES, INC.Year Ended December 31, 1962

See

Airframe	Plane Type	DC-3	Date in Service	Actual Cost	Cost Excluding Built-in Overhaul	Residual (% of Col. 3)	Depreciable Cost (3-4)	Reserve for Depreciation As Reported at 12/31/60	Computed Reserve for Depreciation at 12/31/60	1960 1961 Schad. F 1/4/61/1/1/60 1/2/61/1/1/60 1/3/61/1/1/60	Remaining Service Life Quarters	Quarterly Depreciation Rate (8 + 9)	Computed Depreciation Quarters ended				
													3/31/62	6/30/62	9/30/62	12/31/62	Year End 12/31/62
													11	12	13	14	15
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15			
123,961	85,548	8,554	76,994		4,330	3.33	1,161	1,161	1,161	1,161	887	885	885	885	847	4,330	
118,788	94,162	9,414	84,748		2,218	1.67	1,331	1,331	885	885	917	917	613	613	2,218	3,540	
136,430	95,613	9,560	86,053		4,128	4.67	885	885	917	917	917	917	613	613	3,364		
125,536	87,769	8,678	77,091		3,364	3.67	917	917	917	917	917	917	613	613	877		
116,605	101,605	10,160	91,445		877	3.33	263	263	263	263	263	263	88	88	150		
119,261	104,261	10,426	93,835		150	.33	454	454	150	150					1,038		
128,726	89,531	8,954	80,577		1,038	1.00	1,038	1,038	1,038	1,038					1,038		
170,024	160,024	16,002	144,022		1,359	2.67	509	509	509	509	341	341	408	408	1,359		
174,094	162,231	16,224	146,007		2,176	5.33	408	408	408	408	408	408	408	408	1,632		
For details see 1961 Schedule F																	
Depreciation	on 5 DC-3 added in 1961 and depreciated on a 3 year basis since acquisition									1,050	1,050	1,050	1,050	1,050	4,200		
NC 15748										2,492	2,492	2,492	2,492	2,492	9,968		
NC 28341										2,322	2,322	2,322	2,322	2,322	9,288		
NC 88854										3,033	3,033	3,033	3,033	3,033	2,132		
NC 25651										2,603	2,603	2,603	2,603	2,603	10,412		
NC 33347																	
										18,162	16,530	15,475	14,341	64,508			
Computed Depreciation for 1962																	

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[104]

CAB Form T-70
(11-61)

CLASS RATE PROFIT SHARING SCHEDULE

ADJUSTMENT TO REPORTED INVESTMENT IN FLIGHT EQUIPMENT
AS OF 12/31/64

Year ended December 31, 1962

Carrier NORTH CENTRAL AIRLINES, INC.

Flight Equipment	Reported					Recognized				
	Cost	Reserve for Depreciation	Airworthiness Reserve	Net Book Value (1-2-3)	Undepreciated Cost	Residual Value	Built-in Overhaul Residual	Computed Unrecovered Overhaul	Net Book Value (\$4+5+7+8)	Adjustment (4-9)
DC-3 Airframes	1	2	3	4	5	6	7	8	9	10
38941	123,962	70,607	7,827	45,528	4,330	8,555	30,586	43,471	2,057	
17320	118,788	78,859	7,136*	47,065	2,218	9,416	31,762	43,396	3,669	
17312	136,430	80,302	86	56,042	4,128	9,561	40,732	54,421	1,621	
38943	125,536	72,820	7,138	45,578	3,364	8,677	31,630	43,671	1,907	
26214	113,611	71,527	20,760*	62,844		7,947	54,897	62,844	-	
18949	140,798	82,434	2,531*	60,895		9,159	51,736	60,895	-	
15598	116,605	89,997	10,831	15,777	877	10,160	4,169	15,206	571	
21728	103,740	79,866	13,768	10,106		8,874	1,232	10,106	-	
18196	110,794	86,214	9,430	15,150		9,579	5,571	15,150	-	
28381	110,818	84,909	8,943	16,966		9,434	7,532	16,966	-	
21729	113,849	88,563	3,377	21,909		9,885	11,626	21,511	398	
12978	112,132	85,802	9,334*	35,664		9,713	24,334	34,047	1,617	
28385	111,434	86,678	5,014	19,742		9,643	9,986	19,629	113	
33632	111,051	85,984	2,077	22,990		9,605	12,923	22,528	462	
33633	112,551	86,994	2,000	23,557		9,755	13,000	22,755	802	
15773	119,261	92,356	5,586*	32,491	150	10,426	20,586	31,162	1,329	
12954	112,259	86,456	2,128*	27,931		9,726	17,128	26,854	1,077	
1945	128,726	76,684	15,028	37,014	1,038	8,953	24,166	34,157	2,857	
17318	179,271	128,253	5,830*	56,848		14,250	42,598	56,848	-	
817	170,024	141,476	17,769*	46,317	1,359	16,002	27,769	45,130	1,187	
25648	109,300	87,694	8,804	12,802		9,744	3,058	12,802	-	
25649	174,094	143,150	19,552*	50,496	2,176	16,223	31,415	49,814	682	
408	91,827	50,338	14,733	26,756		6,061	16,482	22,543	4,213	
15748	14,000	700	-	13,300	11,900	1,400	-	13,300	-	
25651	52,950	2,022	1,452	49,476	34,369	4,043	11,064	49,476	-	
88854	38,000	1,548	1,232	35,220	26,312	3,095	5,813	35,220	-	
33347	40,950	1,735	1,333	37,882	29,502	3,471	4,909	37,882	-	
28341	41,700	1,661	1,312	38,727	28,240	3,322	7,165	38,727	-	
TOTAL	3,034,461	2,045,629	23,759	965,073	149,963	246,679	543,869	940,511	24,562	

CAB Form T-88
(11-61)

CLASS RATE PROFIT SHARING SCHEDULE

NONOPERATING INCOME AND EXPENSE NET

Carrier NORTH CENTRAL AIRLINES, INC.Year ended December 31, 1962

Item	Account Number	As Reported per CAB Form 41 Schedule P-3	Adjustment	As Adjusted
Interest charged to construction-credit	8180.1			
Interest charged to development-credit	8180.2			
Capital gains and losses - Operating property	8181.1	554*		554*
Capital gains and losses - other	8181.2			
Unapplied cash discounts	8182	10,554		10,554
Interest income	8183	4,204	63	4,141
Dividend income	8184			
Foreign exchange adjustments	8185			
Income from nontransport ventures	8186			
Interest on debt principal	8187.1	300,367*	300,367*	300,367*
Amortization of discount expense on debt	8187.2	11,636*	11,636*	11,636*
Amortization of premium on debt	8187.3			
Miscellaneous nonoperating credits	8188			
Miscellaneous nonoperating debits	8189	2,852*	2,852*	2,852*
Nonoperating income and expense - net	8199	300,651*	314,792*	14,141

SCHEDULE Q

[107]

[107]

CAB Form T-88
(11-61)CLASS RATE PROFIT SHARING SCHEDULE
INCOME TAX ADJUSTMENT - SUMMARYCarrier NORTH CENTRAL AIRLINES, INC.Year ended December 31, 1962

	Federal	State	Total
1. Pro forma adjusted income for tax purposes, before income tax and profit sharing. (Include gross formula subsidy).....	1,524,454	603.123	
2. Tax related to 1 above per pro forma tax returns submitted herewith	787,216	47,362	834,578
3. <u>Adjustments:</u>			
a) Taxes applicable to capital gains on flight equipment. See Schedule T			
b) Taxes applicable to non-transport ventures. See Schedule S.			
c) Tax effect of retroactive subsidy. See Schedule U.			
d) Total adjustment	787,216	47,362	834,578
4. Adjusted taxes			
<u>State Income Tax Computation</u>	<u>Wisconsin</u>	<u>Minnesota</u>	<u>Iowa</u>
Adjusted Taxable Income	363,051	193,227	40,995
Rate	<u>7% Less \$195</u>	<u>10.23% Less \$260</u>	<u>3%</u>
Tax	25,219	19,767	2,200
The following adjustment is the difference between the taxable income reported on the returns and the amount in item 1. above.			176
Mail subsidy held back for 1962			172,533
Profit sharing for 1962 per form 41 reports			316,225
Mail subsidy held back for 1961 and reported in 1962			(220,304)
			268,454
Tax income per 1 above			1,524,454
Adjusted Form 41 income per Schedule B, line 6			1,909,000
Difference			384,546
Disallowances per schedule C	(89,003)		
Excess depreciation over tax base	39,366		
Excess depreciation - investment credit	2,107		
Extension and development over tax base	47,713		
Addition deduction for pension plan	(32,532)		
Officers life insurance - net of CSV	317		
Adjustments per schedule Q	(314,792)		
State income taxes	(38,600)		
Prior year subsidy adjustment	878		
			384,546

SCHEDULE R

CLASS RATE PROFIT SHARING SCHEDULE

Carrier NORTH CENTRAL AIRLINES, INC.

DEVELOPMENTAL AND PREOPERATING COSTS

Year ended December 31, 1962

	Quarter ended:				
	12/31/61	3/31/62	6/30/62	9/30/62	12/31/62
<u>Investment Adjustment-Prorate</u>					
1. To reflect recognized balance in account 1830 as at 12/31/60	- 167,874				
2. To exclude non-recognized additions to account 1830 (Per V-2)			124	9540	4469
3. Cumulative adjustment (prorate)	- 167,874	- 167,874	- 167,998	- 177,538	- 182,007
<u>Investment Adjustment-to Equity</u>					
4. Reported amortization		22,443	22,443	22,443	25,241
a. Per Form 41, schedule B-10, column 4		22,443	22,443	22,443	25,241
b. Per Form 41, schedule B-10, column 7		12,113	12,113	12,113	12,113
c. Total		10,330	20,660	30,990	44,118
5. Computed amortization per V-2					
6. Investment adjustment (equity) (Line 4c-5) Cumulative..					
<u>Operating Expense Adjustment</u>					
7. Expense adjustment (Line 4c-5)		10,330	10,330	10,330	13,128

SCHEDULE V-1

Schedule V-1

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[108]

[108]

[109]

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CAB Form T-88
(11-61)

CLASS RATE PROFIT SHARING SCHEDULE

DEVELOPMENTAL AND PREOPERATING COSTS

Carrier NORTH CENTRAL AIRLINES, INC.

Year ended December 31, 1962

Docket Number	Extension and Development As of 12/31/60		Additions During 1961 by Quarters				Remaining Quarters at 12/31/61	Amortization Per Quarter (Lower of 1 or 2)	Computed Amortization of Amount Recognized Quarters Ended				
	Reported	Recognized	3/31/62	6/30/62	9/30/62	12/31/62			3/31/62	6/30/62	9/30/62	12/31/62	Yes 12
	1	2	3	4	5	6	7	8	9	10	11	12	13
7067	100												
7050	100												
7141	11,262	11,262						15.67	719	719	719	719	2,876
7697	5,820	5,820						9.33	624	624	624	624	2,496
7454	44,348	20,799						8.67	2,400	2,400	2,400	2,400	9,600
4251	162,072	43,412						15.67	2,770	2,770	2,770	2,770	11,080
CV Integration	52,259	52,259						9.33	5,600	5,600	5,600	5,600	22,400
9891	4,056												
10905	1,436												
11158	20												
11042	19,161												
12583	630												
12849	162												
13391													
13743													
9767													
Use it or lose it cases													
Total	301,426	133,552		124	9,540	5,757			12,113	12,113	12,113	12,113	48,452

SCHEDULE V-2

Schedule V-2

CLASS RATE PROFIT SHARING SCHEDULE
INVESTMENTCarrier NORTH CENTRAL AIRLINES, INC.Year ended December 31, 1962

<u>Reported investment per Form 41</u>	Balance Sheet As At:					Average Investment			
	12/31/61	3/31/62	6/30/62	9/30/62	12/31/62	Long-term Debt	Preferred Equity	Common Equity	Total
Long-term debt	3,846,975	3,884,007	4,293,038	3,956,956	5,135,117	4,156,262			4,156,262
Preferred equity	2,035,562	1,994,592	2,533,563	2,804,728	2,740,726		2,430,257		2,430,257
Common equity	5,882,537	5,878,599	6,826,601	6,761,684	7,875,843				6,586,519
<u>Total</u>									
<u>Adjustments</u>									
<u>Identified as debt or equity:</u>									
1. Notes payable due beyond 90 days	870,490	711,762	1,024,345	1,179,858	1,019,171	965,199			965,199
2. Unamortized discount and expense on debt	-45,542	-42,633	-39,724	-51,704	-49,882	-45,443			-45,443
3. Equipment replacement fund-gains									
4. Capital stock expense				- 3,002	- 3,002		- 1,126	- 1,126	
5. Reserves accrued thru charges to operating expense					107,739		13,467	13,467	
6. Subsidy-retroactive award									
7. Amortization of extension and development-per schedule V-1		10,330	20,660	30,990	44,118		21,010	21,010	
8. Depreciation expense-per schedule E		5,133	9,964	14,148	17,673		9,521	9,521	
9. Maintenance expense-per schedule W/M							- 3,070	- 3,070	
10. Cumulative difference between gross and reported subsidy..				358,000	316,225		129,028	129,028	
11. Inconsistent reporting									
Subtotal	6,682,923	6,563,191	7,841,846	8,289,974	9,327,885	5,076,018	2,599,087	7,675,105	
Debt-equity ratio						66.14	33.86		
<u>Prorated on debt-equity ratio:</u>									
1. Nonoperating property									
2. Investment in affiliate or nontransport activity per schedule D									
3. Cash value of life insurance	-10,994	-10,994	-10,994	-10,994	-14,064				
4. Equipment replacement funds other than gain									
5. Equipment purchase deposits									
6. Capitalized organization expense									
7. Special funds	- 1,000	- 1,000	- 1,000	- 1,000	1,000				
8. Working capital in excess of 3 months' expenses									
9. Construction work in progress									
10. Nonrecognition of capitalized R&D, per schedule V-2	-167,874	-167,874	-167,998	-177,538	-182,007				-172,088
11. Inconsistent reporting									
Total prorated adjustments						- 122,006		- 62,460	- 184,466
Total adjusted investment						4,954,012	2,536,627	7,490,639	

SCHEDULE W

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[110]

[111]

[111]

U.S. CORPORATION INCOME TAX RETURN—1962

FORM 120

U.S. Treasury Department
Internal Revenue Serviceor other taxable year beginning _____, 1962, ending _____, 19_____
(PLEASE TYPE OR PRINT)

- Check if this is a—
 A. Sole proprietorship or
 partnership electing
 under sec. 1361 to be
 taxed as a corporation.
 B. Consolidated return
 C. Parent Holding Co.
 D. Employer Identification
 No.

41-728838

Name **NORTH CENTRAL AIRLINES, INC.**
 Number and street **6201 Thirty-Fourth Avenue, South**
 City or town, postal zone number, State **Minneapolis 50, Minnesota**

E. Business Code No.
(see instructions) **4417**F. County in which located
Eau ClaireG. Enter total assets from line
13 Sch. L (see instr. R.)
14,282,268

IMPORTANT—All applicable lines and schedules must be filled in. If the lines on the schedules are not sufficient, see instruction Q.

GROSS INCOME	1. Gross receipts or gross sales	Less: Returns and allowances	
	2. Less: Cost of goods sold (Schedule A) and/or operations (attach schedule)		
3. Gross profit			
4. Dividends (Schedule C)			
5. Interest on obligations of the United States, etc. issued:			
(a) Prior to 3-1-41			
(b) After 2-28-41			
6. Other interest			
7. Rents			
8. Royalties			
9. Net gains (losses) (from separate Schedule D)			
10. Other income (attach schedule)			
11. TOTAL income, lines 3 to 10, inclusive			
12. Compensation of officers (Schedule E)			
13. Salaries and wages (not deducted elsewhere)			
14. Repairs (do not include cost of improvements or capital expenditures)			
15. Bad debts (from Schedule F if reserve method is used)			
16. Rents			
17. Taxes (attach schedule)			
18. Interest			
19. Contributions or gifts paid (attach schedule—see instructions for limitation)			
20. Losses by fire, storm, shipwreck, or other casualty, or theft (attach schedule)			
21. Amortization (attach schedule)			
22. Depreciation (Schedule G)			
23. Depletion (attach schedule)			
24. Advertising			
25. (a) Pension, profit-sharing, stock bonus, annuity plans (see instructions). (b) Other employee benefit plans (see instructions)			
26. Other deductions (attach schedule)			
27. TOTAL deductions in lines 12 to 26, inclusive			1,253,000
28. Taxable income before net operating loss deduction and special deductions (line 11 less line 27)			
29. Less: (a) Net operating loss deduction (see instructions—attach schedule). (b) Special deductions (Schedule I)			
30. Line 28 less line 29			1,256,500
31. TOTAL income tax (from line 9, Tax Computation Schedule, page 3)			63,925.00
32. Credits: (a) Tax paid with application for extension of time to file (att. Form 7004). (b) Payments and credits on 1962 Declaration of Estimated Tax			
(c) Credit from regulated investment companies (attach Form 2439)			25,659.68
(d) Investment credit (attach Form 3468)			
33. If tax (line 31) is larger than credits (line 32), the balance is TAX DUE. Enter balance here →			89,584.68
34. If tax (line 31) is less than credits (line 32)..... Enter the OVERPAYMENT here →			
35. Enter amount of line 34 you want: Credited on 1963 estimated tax		Refunded	

I declare under the penalties of perjury that I have examined this return (including accompanying schedules and statements) and to the best of my knowledge and belief it is true, correct, and complete. If prepared by a person other than taxpayer, his declaration is based on all information of which he has any knowledge.

31/1963

Treasurer

CORPORATE
SEAL
31/12/1963

(Date)

(Date)

(Signature of officer)

(Individual or firm signature of preparer)

312 East Wisconsin Avenue
Milwaukee 2, Wisconsin

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P-12

Form 1120 (1962)

Schedule H.—SUMMARY OF DEPRECIATION AND AMORTIZATION SCHEDULES

DEPRECIATION	Under Rev. Proc. 61-71 1,305,000	Other	AMORTIZATION
1. Straight line method			1. Emergency facilities.....
2. Declining balance method			2. Research or experimental.....
3. Sum of the years digits method			3. Exploration and development.....
4. Based on units of production			4. Organizational.....
5. Addl. 1st year (Sec. 179)			5. Trademark and trade name.....
6. Other methods	1,305,000		6. Total amortization claimed.....
7. Total depreciation claimed			

Schedule I.—SPECIAL DEDUCTIONS

1. Partially tax-exempt interest (see Instruction 5).....		
2. Dividends received:		
(a) 85 percent of column 2, Schedule C.....		
(b) 62.115 percent of column 3, Schedule C.....		
(c) 85 percent of dividends received from certain foreign corporations.....		
3. Total dividends received deductions (sum of lines 2(a), (b), and (c) but not to exceed 85 percent of the excess of line 28, page 1 over the sum of lines 1 and 5). (See instructions in case of net operating loss or if the corporation is a small business investment company.).....		
4. Dividends paid on certain preferred stock of public utilities (see instructions in case of net operating loss).....		
5. Western Hemisphere trade corporations (see instructions in case of net operating loss).....		
6. Total special deductions (enter here and on line 29(b), page 1).....		

TAX COMPUTATION SCHEDULE

1. (a) Line 30, page 1.....	(b) plus line 1, Schedule I.....	Enter total here → 1,256,000
2. If amount of line 1 is:		
(a) Not over \$25,000—Enter 30 percent of line 1 (32 percent if a consolidated return).....	653,120.00	
(b) Over \$25,000—Enter 52 percent of line 1 (54 percent if a consolidated return).....	5,500.00	647,620.00
Subtract \$5,500, and enter difference.....		
3. Adjustment for partially tax-exempt interest. Enter 30 percent of line 1(b), but not in excess of 30 percent of line 1.....		647,620.00
4. Normal tax and surtax (line 2 less line 3).....		
5. Income tax (line 4, or line 22 of separate Schedule D).....		
6. Credit allowed a domestic corporation for income taxes paid to a foreign country or United States possession (attach Form 1118).....		
7. Balance of income tax (line 5 less line 6).....		
8. Tax under section 541 of the Internal Revenue Code (from Schedule 1120 PH).....		647,620.00
9. Total income tax (line 7 plus line 8). Enter here and on line 31, page 1.....		8,205

H. Date incorporated.

- I. (1) Did the corporation at the end of the taxable year own directly or indirectly 50 percent or more of the voting stock of a domestic corporation?..... Yes No
- (2) Did any corporation, individual, partnership, trust, or association at the end of the taxable year own directly or indirectly 50 percent or more of the corporation's voting stock?..... Yes No (For rules of attribution, see section 267 (c).)
- If the answer to (1) or (2) is "Yes," attach separate schedule showing:
- (a) name and address;
 - (b) percentage owned;
 - (c) date acquired; and
 - (d) the District Director's office in which the income tax return of such organization for the last taxable year was filed.
- If the answer to (1) above is "Yes," include the income (or loss) from line 30, page 1, Form 1120 of such corporation for the taxable year ending with or within your taxable year.
- If the answer to (2) above is "Yes," include (a) the amount of cash or stock dividends paid to such individual or organization and (b) identify form of organization.
- J. Were Forms 1096 and 1097 filed for the calendar year 1962 in connection with:
- Taxable dividends..... Yes No
 - Other payments..... Yes No
- K. Did you have any contracts or subcontracts subject to the Renegotiation Act of 1951?..... Yes No
- If "Yes," see Inst. K. Enter amount here.....
- L. Did you at any time during the year own directly or indirectly any stock of a foreign corporation?..... Yes No
- If "Yes," attach statement as required by Instruction N.

M. Amount of income (or deficit) for: 1959 **1,663,018**
1960.. 1961..

N. If a cooperative association, check type:
(1) farmers' purchasing or marketing; (2) consumers', or (3) other.

O. Did you claim a deduction for expenses connected with: (If answer to any question is "Yes," check applicable boxes within that question.)

(1) A hunting lodge , working ranch or farm , fishing camp , resort property , pleasure boat or yacht , or other similar facility ? (Other than where the operation of the facility was the principal business.) Yes No

(2) The leasing, renting, or ownership of a hotel room or suite , apartment , or other dwelling , which was used by customers or employees or members of their families? (Other than use by employees while in business travel status.) Yes No

(3) The attendance of your employees' families at conventions or business meetings? Yes No

(4) Vacations for employees or members of their families? (Other than vacation pay reported on Form W-2.) Yes No

P. Refer to instructions and state the **Air Transportatio**
Principal business activity

Principal product or service

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FORM 3468

U.S. Treasury Department
Internal Revenue Service

COMPUTATION OF INVESTMENT CREDIT—1962

or taxable year beginning 1962, ending 19

TO BE ATTACHED
TO YOUR
TAX RETURN

Name (as shown on page 1 of your tax return)

NORTH CENTRAL AIRLINES, INC.

Address (number and street)

6201 Thirty-Fourth Avenue, South

City or town, postal zone number, State

Minneapolis 50, Minnesota

1. Qualified investment in new or used property

NOTE: Include your share of investment in property by partnerships, estates, trusts or small business corporations.

Type of property	Line	(1) Life years	(2) Cost or basis	(3) Applicable percentage	(4) Qualified investment (column 2 x column 3)
NEW PROPERTY	(a)	4 to 6	623,747.81	33 1/3	207,913.85
	(b)	6 to 8	161,444.15	66 2/3	107,625.57
	(c)	8 or more	51,027.46	100	51,027.46
USED PROPERTY (for dollar limitation see instructions)	(d)	4 to 6		33 1/3	
	(e)	6 to 8		66 2/3	
	(f)	8 or more		100	

2. Total qualified investment—add lines 1(a) through (f) **366,566.89**
 3. Tentative investment credit—7% of line 2 (for public utility property, enter 3% of line 2) **25,659.68**

COMPUTATION OF TAX FOR PURPOSES OF LIMITATION

4. (a) Individuals (enter amount from line 12, page 1, Form 1040).....	647,620.00
(b) Estates and trusts (enter amount from line 25 or 26, page 1, Form 1041).....	
(c) Corporations (enter amount from line 7, Tax Computation Schedule, Form 1120).....	
5. Individuals, estates and trusts:	
Less: (a) Foreign tax credit.....	
(b) Dividend received credit.....	
(c) Partially tax exempt interest credit	
(d) Retirement income credit.....	
(e) Total (add lines (a), (b), (c) and (d)).....	647,620.00
6. Balance (line 4 less line 5(e)).....	

LIMITATION BASED ON AMOUNT OF TAX

(Married persons filing separately, affiliated groups, estates and trusts—see instructions)

7. (a) Enter amount on line 6 or \$25,000, whichever is lesser.....	25,000.00
(b) If line 6 is in excess of \$25,000, enter 25% of the excess.....	155,655.00
(c) Total (add lines (a) and (b)).....	180,655.00
8. Investment credit (enter amount on line 3 or 7(c), whichever is lesser).....	25,659.68

SCHEDULE A

If any part of the investment in 1 above was made by a partnership, estate, trust, small business corporation, or lessor complete the following:

Name (Partnership, estate, trust, etc.)	Address	Property		
		New	Used	Life years
.....
.....
.....

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North Central Airlines, Inc.

TAXABLE INCOME

Year ended December 31, 1962

INCOME

Transportation revenue	\$27,103,209
Less cost of operations (Schedule 2)	<u>20,651,357</u>
	<u>6,451,852</u>
Loss on disposal of fixed assets (Schedule 3)	(554)
Other income (Schedule 4)	<u>104,113</u>
	<u>6,555,411</u>

EXPENSES

Compensation of officers (Schedule 5)	\$ 207,135
Uncollectible accounts	7,678
Rents and landing fees	1,375,472
Taxes (Schedule 6)	910,316
Interest	312,003
Contributions (Schedule 6)	595
Depreciation and amortization (Schedule 7)	1,305,002
Advertising	356,937
Contributions to pilots' retirement plan "A"	350,394
Other deductions (Schedule 6)	<u>473,879</u>
	<u>5,299,411</u>
Taxable Income — Federal	<u>\$ 1,256,000</u>

Schedule 1

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[115]

North Central Airlines, Inc.

RECONCILIATION OF EARNED SURPLUS TO TAXABLE INCOME

Year ended December 31, 1962

Earned surplus — December 31, 1961	\$ 289,213
Net earnings for the year	<u>534,333</u>
	<u>823,546</u>
Income taxes on 1961 mail subsidy received in 1962	<u>(127,775)</u>
Earned surplus — December 31, 1962	<u><u>\$ 695,771</u></u>
Net earnings per books for year ended December 31, 1962	\$ 534,333
Add	
Excess depreciation over tax base	\$ 39,366
Excess depreciation — investment credit	2,107
Route development and preoperating expense in excess of tax basis	47,713
Provision for pilots' pension plan	317,862
Officers life insurance — net of CSV	317
Mail subsidy held back under C.A.B. profit sharing provision in 1961	220,304
Accrued Federal income taxes	616,725
Overaccrual of States' income taxes	<u>200</u>
	<u><u>1,244,594</u></u>
	<u><u>1,778,927</u></u>
Deduct	
Allowable pilots' pension plan expense	350,394
Mail subsidy held back under C.A.B. Profit sharing provisions 1962	<u>172,533</u>
	<u><u>522,927</u></u>
Taxable income — Federal	<u><u>\$1,256,000</u></u>

Schedule 9

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CIVIL AERONAUTICS BOARD
Washington, D. C.

REPORT OF EARNINGS SUBJECT TO PROFIT-SHARING PURSUANT
TO THE PROVISIONS OF LOCAL SERVICE CLASS SUBSIDY RATE,
DOCKET 12004, ORDER E-16485, AS AMENDED

Twelve months ended December 31, 1962

North Central Airlines, Inc.

(Full name of reporting company)

CERTIFICATION*

I, the undersigned _____
(Title of officer in charge of accounts)

of the _____ North Central Airlines, Inc.
(Full name of the reporting company)

do certify that this report and all schedules and supporting documents which are submitted herewith or have been submitted heretofore as parts of this report filed for the above indicated period have been prepared under my direction; that I have carefully examined them and declare that they correctly reflect the accounts and records of the company, and to the best of my knowledge and belief are a complete and accurate statement of the earnings subject to profit-sharing for the period indicated above, computed in accordance with the provisions of Order E-16485, as amended.

/s/ Bernard Sweet
(Signature)

(Post office address)

Date December 11, 1963

* Section 35(A) of the United States Criminal Code, 18 U.S.C. §80, makes it a criminal offense subject to a maximum fine of \$10,000 or imprisonment for not more than 10 years, or both, to knowingly and wilfully make or cause to be made any false or fraudulent statements or representations in any matter within jurisdiction of any agency of the United States.

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NORTH CENTRAL AIRLINES, INC.

General Offices: 6201 Thirty-Fourth Avenue So.
Minneapolis, Minn. 55450

September 15, 1964

Mr. K. Donaldson
Senior Analyst
Bureau of Economic Regulations
Civil Aeronautics Board
Washington, D. C. (20428)

Dear Mr. Donaldson:

I am enclosing group depreciation schedules for DC-3 and Convair Radio and DC-3 FERPA. These schedules are for 1962 and 1963.

Your auditors have checked these schedules and as far as I know, agreed with them.

I am also enclosing schedules which indicate the book balance in the asset and reserve accounts. These schedules should enable you to reconcile the T88's to our books.

Very truly yours,
NORTH CENTRAL AIRLINES, INC.

/s/ Daniel F. May
Treasurer

DFM/jd
encs.

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[154]

NORTH CENTRAL AIRLINES, INC.

General Offices: 6201 Thirty-Fourth Avenue So.
Minneapolis, Minn. 55450

October 14, 1964

Mr. John B. Russell, Chief
Office of Administration
Civil Aeronautics Board
Washington, D. C. 20428

Dear Mr. Russell:

I am enclosing North Central Airlines amended U.S. Corporate
Income Tax Return for 1962.

As per Mr. Donaldson's request, I am also enclosing a recon-
ciliation of the revenues used in our tax return.

If you have any further questions on these matters, please let
me hear from you.

Very truly yours,
NORTH CENTRAL AIRLINES, INC.

/s/ Daniel F. May
Treasurer

DFM/jd
encs.

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[155]

1962

1963

~~AMENDED~~

FORM 1120

U.S. Treasury Department
Internal Revenue Service

U.S. CORPORATION INCOME TAX RETURN

or other taxable year beginning

1963 ending 19...

(PLEASE TYPE OR PRINT)

- Check if this is a
 Sole proprietorship or
 partnership electing
under sec. 1361 to be
taxed as a corporation.
 Consolidated return
 Personal Holding Co
 Business Code No.
(see instructions)

417

Name

NORTH CENTRAL AIRLINES, INC.

Number and street

6201 Thirty-Fourth Avenue, South

City or town and State

Minneapolis, Minnesota

Postal ZIP code

E. Employer Identification No.

41-728838

F. County in which located.

Hennepin

G. Enter total assets from line
13 Sch I (see instruction R).

14,282,868

IMPORTANT—All applicable lines and schedules must be filed in. If the lines on the schedules are not sufficient, see instruction Q.

GROSS INCOME	1. Gross receipts or gross sales	Less: Returns and allowances	
	2. Loss: Cost of goods sold (Schedule A) and/or operations (attach schedule)		
	3. Gross profit		
	4. Dividends (Schedule C)		
	5. Interest on obligations of the United States and U.S. instrumentalities		
	6. Other interest		
	7. Rents		
	8. Royalties		
	9. Net gains (losses) (from separate Schedule D)		
	10. Other income (attach schedule)		
	11. TOTAL income, lines 3 to 10, inclusive		
12. Compensation of officers (Schedule E)			
13. Salaries and wages (not deducted elsewhere)			
14. Repairs (do not include cost of improvements or capital expenditures)			
15. Bad debts (from Schedule F if reserve method is used)			
16. Rents			
17. Taxes (attach schedule)			
18. Interest			
19. Contributions or gifts paid (attach schedule—see instructions for limitation)	SCHEDULE 1 ATTACHED		
20. Losses by fire, storm, shipwreck, or other casualty, or theft (attach schedule)			
21. Amortization (attach schedule)			
22. Depreciation (Schedule G)			
23. Depletion (attach schedule)			
24. Advertising			
25. (a) Pension, profit-sharing, stock bonus, annuity plans (see instructions)			
(b) Other employee benefit plans (see instructions)			
26. Other deductions (attach schedule)			
27. TOTAL deductions in lines 12 to 26, inclusive		1,035,412	
28. Taxable income before net operating loss deduction and special deductions (line 11 less line 27)			
29. Loss: (a) Net operating loss deduction (see instructions—attach schedule)			
(b) Special deductions (Schedule I)			
30. Taxable income (line 28 less line 29)		1,035,412	
31. TOTAL income tax (from line 10, Tax Computation Schedule, page 3)	13,965.00	532,916.24	
32. Credits: (a) Tax paid with Form 7004 application for extension (attach copy)	621,360.00		
(b) Payments and credits on 1963 Declaration of Estimated Tax	25,659.68	663,584.68	
(c) Credit from Investment credit Form 3468			
33. If tax (line 31) is larger than credits (line 32), the balance is TAX DUE. Enter balance here →		130,670.44	
34. If tax (line 31) is less than credits (line 32). Enter the OVERPAYMENT here →	130,670.44	Refunded	
35. Enter amount of line 34 you want: Credited on 1964 estimated tax			

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief it is true, correct, and complete. If prepared by a person other than taxpayer, his declaration is based on all information of which he has any knowledge.

CORPORATE SEAL

9/1/64

Date

Signature of officer

Treasurer

Title

9/1/64

Alexander G. Newell Company 811 E. Wisconsin Ave. Milwaukee, W

Individual or firm signature of preparer

Address

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Form 1120 (1963)

Page 2

Schedule A.—COST OF GOODS SOLD: (See Instruction 2)
(Where inventories are an income-determining factor)

1. Inventory at beginning of year.....	
2. Merchandise bought for manufacture or sale.....	
3. Salaries and wages.....	
4. Other costs per books (attach schedule).....	
5. Total	
6. Less: Inventory at end of year.....	
7. Cost of goods sold (enter here and on line 2, page 1).....	

1. Was inventory valued at—Cost ; lower of cost or market LIFO ; other ? If other, attach explanation.
 2. Have write-downs been made to inventory? Yes No . If "Yes," were the write-downs computed on the basis of:
 - (a) Percentage reductions from parts of the inventory
 - (b) Percentage reductions from the total inventory
 - (c) Valuation of individual items.
 If "a" or "b" is checked, enter the percentage of write-downs%. For "a," "b," or "c" enter the dollar amount of write-downs \$ **Nominal**. (If not available, estimate and indicate that the figure is an estimate.)
 3. Was the inventory verified by physical count during the year? Yes No . If "No," attach explanation of how the closing inventory was determined.
 4. Was there any substantial change in the manner of determining quantities, costs or valuations between the opening and closing inventories? Yes No . If "Yes," attach explanation.
- NOTE: If a direct answer cannot be given to a question, attach explanation.

Schedule C.—INCOME FROM DIVIDENDS

1. Name of declaring corporation	2. Domestic corporations taxable under chapter 1, Internal Revenue Code	3. Certain preferred stock of public utilities taxable under chapter 1, Internal Revenue Code	4. Foreign corporations	5. Other corporations
Totals.....				
Total of columns 2, 3, 4, and 5.....				
Add amount includable by shareholder of controlled foreign corporation (attach Form 3646).....				
Total (enter here and on line 4, page 1).....				

Schedule D.—Separate Schedule D (Form 1120) should be used in reporting sales or exchanges of property. (See Instruction 8)**Schedule E.—COMPENSATION OF OFFICERS.** (See page 5 of Instructions)

1. Name and address of officer	2. Official title	3. Time devoted to business	Percent of corporation stock owned	6. Amount of compensation	7. Expense account allowances
4. Common	5. Preferred				
SCHEDULE 5 ATTACHED					
Total compensation of officers (enter here and on line 12, page 1).....					

Schedule F.—BAD DEBTS—RESERVE METHOD. (See Instruction 15)

1. Taxable year	2. Trade notes and accounts receivable outstanding at end of year	3. Sales on account	4. Gross amount added to reserve	5. Amount charged against reserve	6. Reserve for bad debts at end of year
1960.....				2,062	
1961.....				9,800	
1962.....				12,571	
1963.....				7,678	

NOTE: Securities which are capital assets and which became worthless within the taxable year should be reported in separate Schedule D.

Schedule G.—DEPRECIATION. (See Instruction 22, page 3)

This schedule is designed for taxpayers using the alternative guidelines and administrative procedures described in Revenue Procedure 62-21 as well as for those taxpayers who wish to continue using procedures authorized prior to the Revenue Procedure. Where double headings appear use the first heading for the new procedure and the second heading for the older procedure.

1. Group and guideline class —OR— Description of property	2. Cost or other basis at beginning of year —OR— Cost or other basis	3. Asset additions in year (amount) —OR— Date acquired	4. Asset retirements in year (amount) (applicable only to Rev. Proc. 62-21)	5. Depreciation allowed or allowable in prior years	6. Method of computing depreciation —OR— Rate (%) or life	7. Class life —OR— Rate (%) or life	8. Depreciation for this year
SCHEDULE 7 ATTACHED							

1. Totals
2. Less: Amount of depreciation claimed in Schedule A and elsewhere on return.....
3. Balance—Enter here and on line 22, page 1.....
4. Cost or other basis of fully depreciated assets still in use.....

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[157]

AMENDED

1952

1953

SCHEDULE D
(Form 1120)

U.S. Treasury Department - Internal Revenue Service

GAINS AND LOSSES FROM SALES OR EXCHANGES OF PROPERTY

Name and address

PART I.—GAIN FROM DISPOSITION OF DEPRECIABLE PROPERTY UNDER SECTION 1248

a. Kind of property (if necessary, attach statement of descriptive details not shown below)	b. Date acquired (mo., day, yr.)	c. Date sold (mo., day, yr.)	d. Gross sales price	e. Cost or other basis, cost of enhancement improvements (if not purchased, attach explanation) and expense of sale
1.				

f. Depreciation allowed (or allowable) since acquisition or March 1, 1913 (attach schedule)	g. Adjusted basis (e less sum of f-1 and f-2)	h. Total Gain (d less g)	i. Ordinary Gain (greater of f-2 or h)	j. Other Gain (h less i)
f-1. Prior to January 1, 1952	f-2. After December 31, 1951			

2. Total ordinary gain. Enter here and on line 11 and identify as gain from Part I.....

3. Total other gain. Enter here and on line 4 and identify as gain from Part I.....

PART II.—SALE OR EXCHANGE OF PROPERTY UNDER SECTION 1231

a. Kind of property (if necessary, attach statement of descriptive details not shown below)	b. Date acquired (mo., day, yr.)	c. Date sold (mo., day, yr.)	d. Gross sales price	e. Depreciation allowed (or allowable) since acquisition or March 1, 1913 (attach schedule)	f. Cost or other basis, cost of enhancement improvements (if not purchased, attach explanation) and expense of sale	g. Gain or loss (d plus e less f)
4.						

5. Total (If gain, enter on line 9; if loss, enter on line 11. Identify as gain or loss from Part II.).....

PART III.—CAPITAL ASSETS
Short-Term Capital Gains and Losses—Assets Held for Not More Than 6 Months

6.						

7. Unused capital loss carryover from five preceding taxable years (attach statement).....

8. Total of short-term capital gains or losses or difference between short-term capital gains and losses.....

Long-Term Capital Gains and Losses—Assets Held for More Than 6 Months

9.						

10. Total of long-term capital gains or losses or difference between long-term capital gains and losses.....

PART IV.—PROPERTY OTHER THAN CAPITAL ASSETS

11.						

SCHEDULE 3 ATTACHED

(354)

12. Total net gain (or loss). Enter here and on line 15.....

(354)

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Schedule D (Form 1120) 1963

PART V.—TOTAL SCHEDULE D GAINS AND LOSSES

13. Enter the excess of net short-term capital gain (line 8) over net long-term capital loss (line 10)	
14. Enter the excess of net long-term capital gain (line 10) over net short-term capital loss (line 8)	
15. Net gain (loss) from property other than capital assets (line 12)	
16. Total lines 13, 14 and 15, enter here and on Form 1120, page 1, line 9.....	(554) <u>(554)</u>

Alternative Tax Computation

17. Taxable income (line 30, page 1, Form 1120).....	
18. Net long-term capital gain reduced by any net short-term capital loss (line 14).....	
19. Line 17 minus line 18.....	
20. If amount of line 19 is:	
(a) Not over \$25,000—Enter 30 percent of line 19 (32 percent if a consolidated return)	
(b) Over \$25,000—Enter 52 percent of line 19 (54 percent if a consolidated return)	
Subtract \$5,500 and enter difference.....	5,500.00
21. 25 percent of line 18.....	
22. Alternative tax (line 20 plus line 21). If applicable, enter on line 3, Tax Computation, page 3, Form 1120.....	

INSTRUCTIONS (Continued from reverse side of original)

Gains and losses from involuntary conversion and from the sale or exchange of certain property used in the trade or business.—The term "property used in the trade or business," as used in section 1231, means property which has been held more than 6 months, which is used in the trade or business, and which is either real property or property subject to depreciation under section 167, and which is not (a) property of a kind which would properly be includable in the inventory of the taxpayer if on hand at the close of the taxable year, (b) property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business, or (c) certain copyrights or similar properties. Such term also includes timber and coal with respect to which section 631 applies as well as unharvested crops to which section 1231(b)(4) applies. Such term also includes livestock (but not poultry) held for draft, breeding, or dairy purposes and held for 12 months or more from the date of acquisition.

Section 1231 provides special treatment for the gains and losses upon the sale or exchange of "property used in the trade or business" and upon the compulsory or involuntary conversion of (1) such property and (2) capital assets held for more than 6 months. Such gains and losses during the taxable year are treated as gains and losses from the sale or exchange of capital assets held for more than 6 months, if the aggregate of such gains exceeds the aggregate of such losses. If, however, such gains do not exceed such losses, such gains and losses shall not be treated as gains and losses from the sale or exchange of capital assets.

In determining whether gains do or do not exceed losses, it is necessary to include the gains and losses to the extent that they would be included if they were all ordinary gains and losses. The limitation of section 1211 on the deductibility of capital losses does not operate to exclude any such losses from the computation as to the excess of gains over losses, but all such losses are included in full. The total shown on line 5 determines whether the items reflected therein represent a long-term capital gain or an ordinary loss. The total must be entered on the first line of the appropriate Schedules of Part III or Part IV.

For special treatment of gain or loss upon the cutting of timber, or upon the disposal of timber or coal under a contract by which the owner retains an economic interest in such timber or coal, see section 631.

Long-term capital gains from regulated investment companies.—Include in income as a long-term capital gain the amount the corporation has been notified constitutes its share of the undistributed capital gains of a regulated investment company.

Alternative tax.—If for any taxable year the net long-term capital gain exceeds the net short-term capital loss, or if there is only a net long-term capital gain, section 1201 imposes an alternative tax in lieu of the normal tax and surtax imposed upon taxable income, if any, only if such tax is less than the tax imposed by section 11 (relating to normal tax and surtax on corporations),

sections 821 and 831 (relating to normal tax and surtax on insurance companies, other than life insurance companies), or section 511(a)(1) (relating to taxation of business income of certain organizations described in section 511(a)(2)). The alternative tax is the sum of (1) a partial tax, computed at the normal tax and surtax rates on the taxable income decreased by the amount of the excess of the net long-term capital gain over the net short-term capital loss, and (2) 25 percent of such excess.

If the corporation computes an alternative tax under section 1201 and is entitled to special deductions for dividends received (sections 243, 244, 245), the special deduction for dividends paid (section 247), the special deduction for a Western Hemisphere trade corporation (section 922), or the special deduction for a China Trade Act corporation (section 941), such special deductions are to be based upon taxable income including the excess of net long-term capital gain over net short-term capital loss.

Bonds, etc., losses of banks.—In the case of a bank, as defined in section 581, if the losses in the taxable year from sales or exchanges of bonds, debentures, notes, or certificates, or other evidences of indebtedness, issued by any corporation (including one issued by a government or political subdivision thereof) exceed the gains from such sales or exchanges, such excess shall be considered as an ordinary loss and deductible in full against other income. Section 582.

Dealers in securities. Capital gains and ordinary losses.—Under the provisions of section 1236, gain by a dealer in securities from the sale or exchange of a security, as defined in section 1236, shall in no event be considered as gain from the sale or exchange of a capital asset unless (a) the security was, before the expiration of the thirtieth day after the date of its acquisition, clearly identified in the dealer's records as a security held for investment or, if acquired before October 20, 1951, was so identified before November 20, 1951; and (b) the security was not, at any time after the expiration of such thirtieth day, held by the dealer primarily for sale to customers in the ordinary course of trade or business. A loss from the sale or exchange of a security shall, if section 582(c) is not applicable, be considered a capital loss if at any time after November 19, 1951, the security was clearly identified in the dealer's records as a security held for investment.

Short sales of capital assets.—For rules regarding tax consequences of certain short sales of stock or other securities (including those dealt with on a "when issued" basis), and transactions in commodity futures, see section 1233.

Instructions For Insurance Companies Using This Schedule

Companies taxable under section 831 and having losses from capital assets sold or exchanged in order to obtain funds to meet abnormal insurance losses, etc., shall attach a schedule corresponding to Schedule A-3, Form 1120M. For companies taxable under section 821, all references to "line" numbers, Form 1120, shall be considered as references to the appropriate "line" in Form 1120M.

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AMENDED

FORM 3468

U.S. Treasury Department
Internal Revenue Service

COMPUTATION OF INVESTMENT CREDIT

1962

or taxable year beginning

1962 ending

1962

TO BE ATTACHED
TO YOUR
TAX RETURN

Name (as shown on page 1 of your tax return)

NORTH CENTRAL AIRLINES, INC.

Address (number and street)

6201 Thirty-Fourth Avenue, South

City or town, and State

Minneapolis 50, Minnesota

1. Qualified investment in new or used property

NOTE: Include your share of investment in property by a partnership, estate, trust, small business corporation, or lessor.

Type of property	Line	(1) Life years	(2) Cost or basis	(3) Applicable percentage	(4) Qualified investment (column 2 x column 3)
NEW PROPERTY	(a)	4 to 6	623,747.81	33 1/3	207,913.86
	(b)	6 to 8	161,444.15	66 2/3	107,625.57
	(c)	8 or more	51,027.46	100	51,027.46
USED PROPERTY (for dollar limitation see instructions)	(d)	4 to 6		33 1/3	
	(e)	6 to 8		66 2/3	
	(f)	8 or more		100	

2. Total qualified investment—add lines 1(a) through (f).
3. Tentative investment credit—7% of line 2 (for public utility property, enter 3% of line 2).
4. Carryback and carryover of unused credit(s) (attach statement).
5. TOTAL (line 3 plus line 4).

COMPUTATION OF TAX FOR PURPOSES OF LIMITATION

6. (a) Individuals (enter amount from line 12, page 1, Form 1040).
- (b) Estates and trusts (enter amount from line 25 or 26, page 1, Form 1041).
- (c) Corporations (enter amount from line 5, Tax Computation Schedule, Form 1120).
7. Individuals, estates and trusts:
- Less: (a) Foreign tax credit
- (b) Dividends received credit
- (c) Retirement income credit
- (d) Total (add lines (a), (b), and (c)).
8. Balance (line 6 less line 7(d)).

LIMITATION BASED ON AMOUNT OF TAX

(Married persons filing separately, affiliated groups, estates and trusts—see instructions)

9. (a) Enter amount on line 8 or \$25,000, whichever is lesser
- (b) If line 8 is in excess of \$25,000, enter 25% of the excess
- (c) Total (add lines (a) and (b)).
10. Investment credit (enter amount on line 5 or 9(c), whichever is lesser).

SCHEDULE A

If any part of the investment in 1 above was made by a partnership, estate, trust, small business corporation, or lessor complete the following:

Name (Partnership, estate, trust, etc.)	Address	Property		
		New	Used	Life years
		\$	\$	

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AMENDED

North Central Airlines, Inc.
INDEX TO SCHEDULES ATTACHED
Year ended December 31, 1962

	<u>Schedule Number</u>
TAXABLE INCOME - FEDERAL RETURN	1
COST OF OPERATIONS	2
LOSS ON DISPOSAL OF FIXED ASSETS	3
OTHER INCOME	4
COMPENSATION OF OFFICERS	5
TAXES	6
CONTRIBUTIONS	6
OTHER DEDUCTIONS	6
FIXED ASSETS AND ACCUMULATED DEPRECIATION	7
BALANCE SHEET	8
RECONCILIATION OF EARNED SURPLUS TO TAXABLE INCOME	9

Y AVAILABLE

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North Central Airlines, Inc.

AMENDED CORPORATE TAX RETURN

Year ended December 31, 1962

Based upon a final determination by the Civil Aeronautics Board of the class rate subsidy for year 1961, an amended return was filed in September, 1964, the year of final settlement. It reflected the booking of certain C.A.B. adjustments. Since year 1962 is also affected in part by the 1961 adjustments, an amended return is hereby submitted reflecting the changes to taxable income. R.A.R. dated April 3, 1964 showing additional taxable income of \$30,701 is also reflected in this amended return.

The reconciliation of taxable income per original return to taxable income as amended herein (Schedule 9) is coded to the explanation of adjustments as follows:

- (1) Non-Deductible corporate and fiscal expenses of \$8,181 consists of \$6,572 per R.A.R. dated April 3, 1964 and \$1,609 credited to Account 6840 in 1963, but applicable to 1962. Adjustment is shown in Schedule 6 - Other Deductions.
- (2) Rental of certain O'Hare Field facilities capitalized per R.A.R. of April 3, 1964 of which \$32,172 represents reduction of rent expense for 1962 - Schedule 1.
- (3) Financing costs of \$1,472.83 were capitalized in 1963; should be a 1962 adjustment. An additional \$357 applicable to the 1963 debenture issue is being credited to Account 68360 - Personnel Expense per Schedule 2.
- (4) Extension and development items originally capitalized in 1962 but corrected per amended 1961 return:

<u>Docket Number</u>	<u>Amount</u>
12849	\$ 1,516.60
10905	1,023.57
13391	949.63
11042	126.08
12202	152.25
	<hr/>
	\$ 3,768.13

Items capitalized in 1963;
should be 1962:

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<u>Account Number</u>	<u>Amount</u>
18329	\$ (5,998.13)
18331	(1,650.96)
18336	(1,557.09)
18333	(737.86)
18332	(301.04)
18330	(63.49)
18334	(3,080.90)
Columbus case	(1,369.29)
18316	<u>(1,486.20)</u>
Subtotal	<u>(16,244.96)</u>
Per Schedule 6	<u>\$ (12,476.83)</u>

- (5) Overaccrual of States income taxes per original return:
- | | |
|----------------|-----------------|
| Wisconsin | \$ 3,470 |
| Minnesota | 4,542 |
| North Dakota | 535 |
| Iowa | (7) |
| Ontario | (50) |
| Per Schedule 6 | <u>\$ 8,490</u> |
- (6) Depreciation adjustments as follows:
- | | |
|--|-----------------|
| Depreciation on O'Hare facilities capitalized by
R.A.R. of April 3, 1964 | \$ 8,043 |
| Change in depreciation rates per C.A.B.: | |
| Assemblies and spare parts - DC 3
(item also adjusted in amended 1961 return) | (7,309) |
| Radio equipment (item also adjusted in
amended 1961 return) DC 3 | 11,706 |
| Radio equipment - Convair | <u>(11,563)</u> |
| Per Schedule 7 | <u>\$ 877</u> |
- (7) Reversal of 1961 public service subsidy held by government at December 31, 1962 but received in 1962 and included in income in original return. Amended return filed in 1964 for 1961 reflected the final adjustment of subsidy in 1961. (Schedule 1 - Transportation Revenue).
- (8) Interline payables added to 1961 income per amended return as required in final C.A.B. subsidy determination was included in original 1962 return as filed, and is hereby reversed - (Schedule 1 - Transportation Revenue).

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- (9) Reversal of repair item originally capitalized in 1962 for \$8,719 but adjusted to 1961 per amended return - Schedule 2.
- (10) Workmens Compensation insurance return premiums recorded as 1962 income per original return as filed but adjusted to 1961 per amended return - Schedule 2.
- Request is hereby made to apply the refund of \$130,670.44 to the third quarterly payment of the 1964 1120-ES.

AMENDED

North Central Airlines, Inc.

TAXABLE INCOME

Year ended December 31, 1962

	<u>Per Original Return</u>	<u>Adjustments</u>	<u>Per Amended Return</u>
INCOME			
Transportation revenue	\$27,103,209	\$ (269,732)	\$26,833,477
Less cost of operations (Schedule 2)	<u>20,651,357</u>	<u>11,299</u>	<u>20,662,656</u>
	<u>6,451,852</u>	<u>(281,031)</u>	<u>6,170,821</u>
Loss on disposal of fixed assets (Schedule 3)	(554)		(554)
Other income (Schedule 4)	<u>104,113</u>	<u>(281,031)</u>	<u>104,113</u>
	<u>6,555,411</u>		<u>6,274,380</u>
EXPENSES			
Compensation of officers (Schedule 5)	\$ 207,135	\$ 207,135	
Uncollectible accounts	7,678	7,678	
Rents and landing fees	1,375,472	<u>\$(32,172)</u>	1,343,300
Taxes (Schedule 6)	910,316	(8,490)	901,826
Interest	312,003		312,003
Contributions (Schedule 6)	595		595
Depreciation and amortization (Schedule 7)	1,305,002	877	1,305,879
Advertising	356,937		356,937
Contributions to pilots' retirement plan "A"	350,394		350,394
Other deductions (Schedule 6)	<u>473,879</u>	<u>5,299,411</u> <u>(20,658)</u> <u>60,443</u>	<u>453,221</u> <u>5,238,968</u>
Taxable income — Federal	<u>\$ 1,256,000</u>	<u>\$(220,588)</u>	<u>\$ 1,035,412</u>

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AMENDED

North Central Airlines, Inc.

COST OF OPERATIONS

Year ended December 31, 1962

	<u>Per Original Return</u>	<u>Adjustments</u>	<u>Per Amended Return</u>
Salaries and wages	\$13,307,200	\$ -	\$13,307,200
Personnel expense	700,088	(1,116)	698,972
Aircraft fuel and oil	2,326,431	-	2,326,431
Repair and maintenance	1,673,433	8,719	1,682,152
Insurance	395,046	3,696	398,742
Communications purchased	726,520	-	726,520
Other supplies	155,704	-	155,704
Outside services	357,624	-	357,624
Shop servicing supplies	165,703	-	165,703
Injuries, loss and damage	12,649	-	12,649
Light, heat, power and water	148,923	-	148,923
Other expenses	48,988	-	48,988
Obsolescence on spare parts	20,136	-	20,136
Passenger food service	236,929	-	236,929
Interrupted trip expense	51,168	-	51,168
Commissions - traffic and general	268,617	-	268,617
Traffic schedules and time tables	59,344	-	59,344
Expenses transferred	<u>(3,146)</u>	<u>-</u>	<u>(3,146)</u>
	<u>\$20,651,357</u>	<u>\$11,299</u>	<u>\$20,662,656</u>

Schedule 2

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AMENDED

North Central Airlines, Inc.

LOSS ON DISPOSAL OF FIXED ASSETS

Year ended December 31, 1962

	<u>Cost</u>	<u>Accumulated Depreciation</u>	<u>Cash Received</u>	<u>Gain or (Loss)</u>
Aircraft engines	\$2,696.06	\$2,426.45	\$ -	\$(269.61)
Hangar, shop and ramp equipment	518.50	458.62	217.48	157.60
Maintenance and engineering equipment	885.28	679.26	100.00	(106.02)
Furniture, fixtures and office equipment	2,601.66	2,199.06	55.00	(347.60)
Improvements to leased property	<u>2,227.62</u>	<u>2,227.62</u>	<u>12.00</u>	<u>12.00</u>
	<u>\$8,929.12</u>	<u>\$7,991.01</u>	<u>\$384.48</u>	<u>\$(553.63)</u>

Schedule 3

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AMENDED

North Central Airlines, Inc.

OTHER INCOME

Year ended December 31, 1962

General commissions and service sales	\$46,625
Rent	15,141
Miscellaneous freight income	17,892
Unapplied cash discounts	10,554
Interest	4,204
Other incidental revenue	<u>9,697</u>
	<u>\$104,113</u>

Schedule 4

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AMENDED

North Central Airlines, Inc.
COMPENSATION OF OFFICERS
Year ended December 31, 1962

	<u>Compensation</u>	<u>Expense Allowance</u>
Arthur E. A. Mueller Chairman of the Board	\$ 30,729.31	\$12,648.46
H. N. Carr President	42,583.44	5,664.55
Frank N. Buttomer Vice President	18,625.00	4,301.45
Bernard Sweet Vice President and Treasurer	18,087.50	1,000.52
A. E. Schwandt Vice President	14,425.00	827.79
Ruric H. Bendio Vice President	17,125.00	524.78
Alvin Niemeyer Vice President	12,000.00	293.86
A. L. Wheeler Vice President	27,000.00	27,562.42
John P. Dow Secretary	9,410.00	385.30
D. F. May Assistant Treasurer	9,447.50	1,174.17
Charlotte G. Westberg Assistant Secretary	<u>7,702.50</u>	<u>421.79</u>
	<u>\$207,135.25</u>	

Schedule 5

AMENDED

North Central Airlines, Inc.

TAXES, CONTRIBUTIONS AND OTHER DEDUCTIONS

Year ended December 31, 1962

	<u>Per Original Return</u>	<u>Adjustments</u>	<u>Per Amended Return</u>
TAXES			
Property taxes	\$ 78,771	\$ -	\$ 78,771
Social security	297,456	-	297,456
States unemployment	59,721	-	59,721
Federal unemployment	53,022	-	53,022
Gasoline tax and sundry	380,574	-	380,574
States' income taxes	38,800	(8,490)	30,310
States' sales tax	1,972	-	1,972
	<u>\$910,316</u>	<u>\$(8,490)</u>	<u>\$901,826</u>
CONTRIBUTIONS			
United Fund	\$ 300	\$ -	\$ 300
Junior Achievement of Minneapolis	50	-	50
Sacred Heart Convent	120	-	120
Y.M.C.A. of Minneapolis	75	-	75
Citizens League, Minneapolis-Hennepin	50	-	50
	<u>\$ 595</u>	<u>\$ -</u>	<u>\$ 595</u>
OTHER DEDUCTIONS			
Stationery and office supplies	\$261,005	\$ -	\$261,005
Memberships	26,953	-	26,953
Clearance, customs, duties	14,003	-	14,003
Professional fees	82,576	-	82,576
Corporate and fiscal	25,235	(8,181)	17,054
Foreign exchange	7,282	-	7,282
Extension and development	44,857	(12,477)	32,380
Promotional and publicity expense	7,238	-	7,238
Sundry	4,730	-	4,730
	<u>\$473,879</u>	<u>\$(20,658)</u>	<u>\$453,221</u>

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North Central Airlines, Inc.

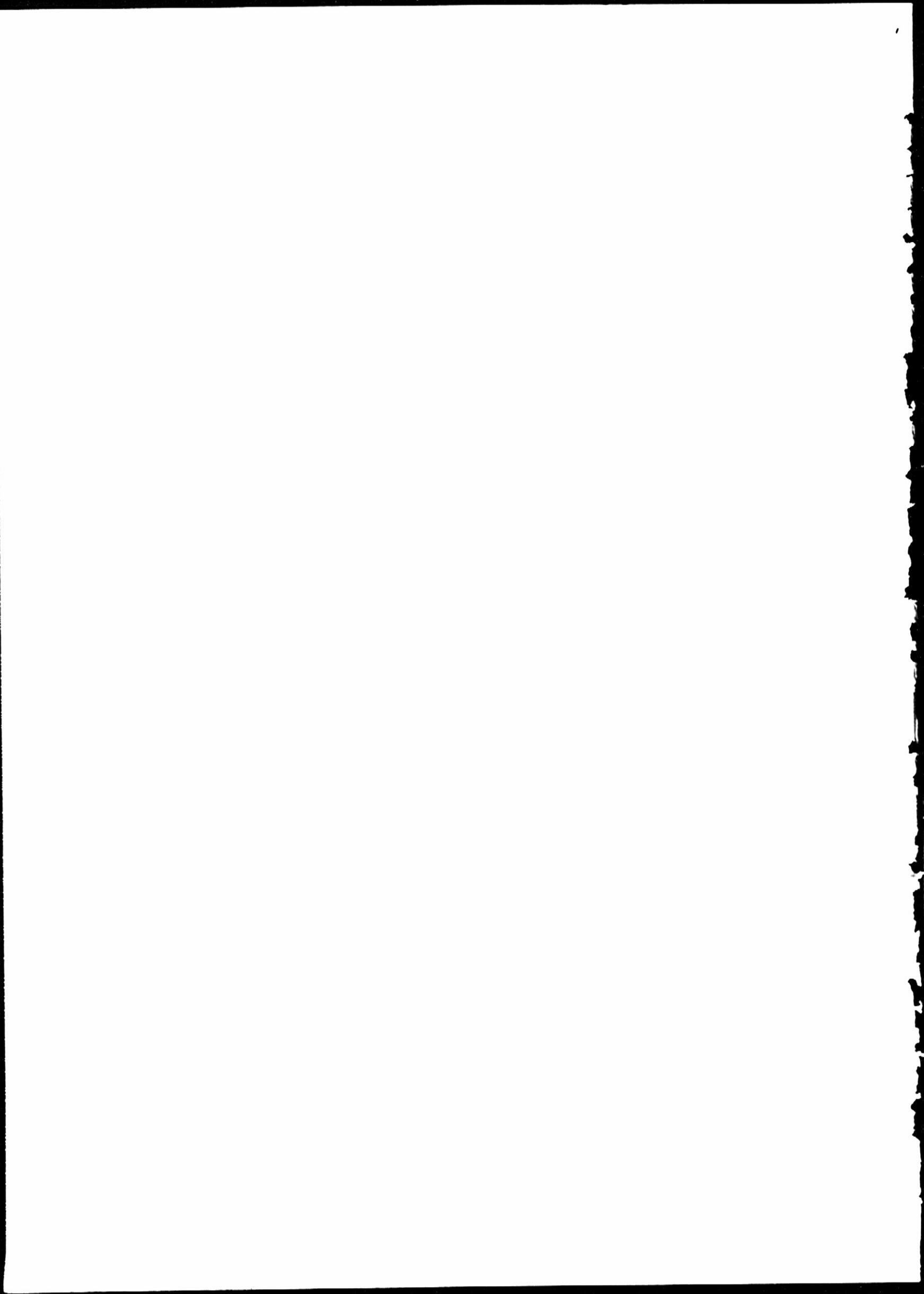
AMENDED

FIXED ASSETS AND ACCUMULATED DEPRECIATION

December 31, 1962

	ASSETS					ACCUMULATED DEPRECIATION				
	December 31, 1961	Additions	Retirements	Transfers in (out)	December 31, 1962	December 31, 1961	Current Provision	Retirements	Transfers in (out)	December 31, 1962
Aircraft										
DC 3's	\$ 3,034,462	\$ 32,799	\$ -	\$ 7,159	\$ 3,074,420	\$ 2,069,387	\$ 284,977	\$ 57,170	\$ -	\$ 2,297,194
Convairs	3,185,715	1,655,491	-	46,110	4,887,316	582,698	527,162	128,333	-	981,527
Engines										
DC 3's	119,971	-	5,256	-	114,715	105,934	720	4,730	-	101,924
Convairs	524,646	247,075	-	(846)	770,875	128,162	73,855	-	-	202,017
Propellers										
DC 3's	26,081	-	-	-	26,081	23,358	115	-	-	23,473
Convairs	158,257	76,057	14,133	-	220,181	26,911	21,296	14,133	-	34,074
Radio equipment										
DC 3's	561,988	65,716	2,961	(50,390)	574,353	492,356	60,034	2,961	(20,806)	528,623
Convairs	377,317	96,630	-	72,783	546,730	67,459	44,602	-	20,806	132,867
Improvements to leased aircraft	33,491	-	27,594	-	5,897	27,807	5,504	27,594	-	5,717
Assemblies and spare parts										
DC 3's	177,227	8,395	3,966	-	181,656	137,406	23,114	4,340	-	156,180
Convairs	424,699	102,475	7,619	74,623	594,178	64,834	56,741	7,691	-	113,884
Station communications and meterological equipment										
Hangar, shop & ramp equip.	284,835	2,714	2,352	3,168	288,365	187,844	23,334	2,352	6	208,832
Furniture, fixtures and office equipment	357,591	110,786	519	(28,129)	439,729	165,670	60,029	459	(14,637)	210,603
Storage and distribution equipment										
Improvements to leased property	261,624	53,992	2,602	(529)	312,485	93,165	25,306	2,205	(44)	116,222
Maintenance and engineering equipment	48,185	15,574	-	-	63,759	34,331	3,951	-	-	38,282
Miscellaneous ground equip.										
Leasehold improvements	136,047	149,008	-	(87,110)	197,945	52,312	51,516	-	31	103,859
Construction in progress	242,216	40,754	885	32,071	314,156	144,045	35,795	681	14,675	193,834
Improvements - long-term lease	8,991	518	-	209	9,718	6,136	1,671	-	-	7,807
Work in process - other	61,711	76,976	-	30,211	168,898	45,927	26,988	-	-	72,915
Passenger service equip.	32,028	549,389	-	(75,594)	505,823	-	-	-	-	-
PER BOOKS	214,892	2,227	56,899	269,564	-	19,557	2,227	(31)	17,299	
Excess of book deprec. over allowable tax basis	5,355	81,012	-	(80,635)	5,732	-	-	-	-	
Aircraft - DC 3's										
Engines - DC 3's										
TOTALS BEFORE INVESTMENT CREDIT	10,062,437	3,588,778	70,114	-	13,581,101	4,465,457	1,307,986	254,876	-	5,518,567
INVESTMENT CREDIT - 1962 additions										
4 to 6		(13,854)			(13,854)		(1,481)			(1,481)
6 to 8		(7,534)			(7,534)		(465)			(465)
Over 8		(3,572)			(3,572)		(161)			(161)
	<u>\$10,062,437</u>	<u>\$ 3,563,818</u>	<u>\$ 70,114</u>	<u>\$ -</u>	<u>\$13,556,141</u>	<u>\$ 4,465,457</u>	<u>\$1,305,879</u>	<u>\$254,876</u>	<u>\$ -</u>	<u>\$ 5,516,460</u>

Schedule 7



AMENDED

North Central Airlines, Inc.

BALANCE SHEET

December 31, 1962 and 1961

<u>ASSETS</u>	<u>1961</u>	<u>1962</u>	<u>LIABILITIES</u>	<u>1961</u>	<u>1962</u>
CURRENT ASSETS			CURRENT LIABILITIES		
Cash	\$ 793,964	\$ 427,784	Notes Payable	\$ 1,104,965	\$ 1,090,884
Accounts receivable	3,134,624	3,423,139	Accounts payable	2,570,059	3,293,334
Operating supplies	1,000,068	1,262,753	Unearned transportation revenue	223,972	161,096
Prepaid expenses and sundry deposits	<u>424,596</u>	<u>582,947</u>	Income taxes	178,000	602,365
	<u>5,353,252</u>	<u>5,696,623</u>	Accrued liabilities	<u>1,480,187</u>	<u>1,140,788</u>
				<u>5,557,183</u>	<u>6,288,467</u>

OPERATING PROPERTY

AND EQUIPMENT - at cost

Fixed assets (Schedule 7 and 8)	10,057,082	13,614,642
Less accumulated depreciation	<u>4,455,742</u>	<u>5,538,658</u>
	<u>5,601,340</u>	<u>8,075,984</u>

Deposit on construction in progress - leased facilities 89,035 -

DEFERRED CHARGES

Route development and pre-operating expense

Rentals	-	201,361	Common stock	1,729,265	1,746,407
Other	<u>94,668</u>	<u>83,599</u>	Capital surplus	<u>17,085</u>	<u>298,548</u>
	<u>396,094</u>	<u>510,261</u>	Retained earnings	<u>289,213</u>	<u>695,771</u>

<u>\$11,439,721</u>	<u>\$14,282,868</u>
---------------------	---------------------

NON-CURRENT LIABILITIES	
Non-current portion of notes payable	3,846,975
Deferred taxes	<u>-</u>
	<u>3,846,975</u>

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Schedule 8

AMENDED

North Central Airlines, Inc.

RECONCILIATION OF EARNED SURPLUS TO TAXABLE INCOME

Year ended December 31, 1962

Earned surplus - December 31, 1961	\$ 289,213
Net earnings for the year	<u>534,333</u>
	823,546
Income taxes on 1961 mail subsidy received in 1962	(127,775)
Earned surplus - December 31, 1962	<u>\$ 695,771</u>
Net earnings per books for year ended December 31, 1962	\$ 534,333
Add	
Excess depreciation over tax base	\$ 39,366
Excess depreciation - investment credit	2,107
Route development and preoperating expenses in excess of tax basis	47,713
Provision for pilots' pension plan	317,862
Officers' life insurance - net of CSV	317
Mail subsidy held back under C.A.B. profit sharing provision in 1961	220,304
Accrued Federal income taxes	616,725
Overaccrual of States' income taxes	<u>200</u> <u>1,244,594</u>
	1,778,927
Deduct	
Allowable pilots' pension plan expense	350,394
Mail subsidy held back under C.A.B. profit sharing provisions 1962	<u>172,533</u> <u>522,927</u>
Taxable income-Federal-Original Return	1,256,000
Add amendments	
Non-deductible corporate and fiscal expense (1)	8,181
Rental capitalized (2)	32,172
Personnel expense adjustment (3)	1,116
Extension and development (4)	12,477
Accrual for states' income taxes (5)	<u>8,490</u> <u>62,436</u>
	1,318,436
Deduct	
Depreciation due to change in rates and capitalization of exp. (6)	877
Final determination of mail subsidy for 1961 (7)	220,304
Interline payable (8)	49,428
Repairs and maintenance capitalized (9)	8,719
Insurance adjustment (10)	<u>3,696</u> <u>283,024</u>
Taxable Income-Federal-Amended Return	<u>\$1,035,412</u>

North Central Airlines, Inc.

Year ended December 31, 1962

ANSWERS TO ITEM I(2), Page 3, Form 1120

- (1) Arthur E. A. Mueller
Mueller Building
Wausau, Wisconsin
- (2) Approximately 55%
- (3) Acquired at various dates
- (4) Milwaukee, Wisconsin

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Form 1120 (1963)

Schedule H.—SUMMARY OF DEPRECIATION AND AMORTIZATION SCHEDULES

DEPRECIATION	Under Rev. Proc. 62-21	Other	AMORTIZATION
1. Straight line method.....			1. Emergency facilities.....
2. Declining balance method.....			2. Research or experimental.....
3. Sum of the years-digits method.....			3. Exploration and development.....
4. Based on units of production.....			4. Organizational.....
5. Addl. 1st year (Sec. 179).....			5. Trademark and trade name.....
6. Other (specify).....			6. Other (specify).....
7. Total depreciation claimed.....			7. Total amortization claimed.....

Schedule I.—SPECIAL DEDUCTIONS

1. Dividends-received: (a) 85 percent of column 2, Schedule C.....	
(b) 62.115 percent of column 3, Schedule C.....	
(c) 85 percent of dividends received from certain foreign corporations.....	
2. Total dividends-received deductions (sum of lines 1(a), (b), and (c) but not to exceed 85 percent of the excess of line 28, page 1 over line 4 of this schedule). (The 85 percent limitation does not apply to a year in which a net operating loss occurs or if the corporation is a small business investment company.).....	
3. Dividends paid on certain preferred stock of public utilities (see instructions in case of net operating loss).....	
4. Western Hemisphere trade corporations (not allowable in year of net operating loss).....	
5. Total special deductions (enter here and on line 29(b), page 1).....	

TAX COMPUTATION SCHEDULE

1. Taxable income (line 30, page 1).....	1,035,412
2. If amount of line 1 is:	
(a) Not over \$25,000—Enter 30 percent of line 1 (32 percent if a consolidated return).....	538,414.24
(b) Over \$25,000—Enter 52 percent of line 1 (54 percent if a consolidated return).....	5,500.00
Subtract \$5,500, and enter difference.....	532,914.24
3. Income tax (line 2, or line 22 of separate Schedule D, whichever is lesser).....	
4. Foreign tax credit (attach Form 1118).....	
5. Balance (line 3 less line 4).....	532,914.24
6. Investment credit (attach Form 3468).....	
7. Balance of income tax (line 5 less line 6).....	
8. Tax under section 541 of the Internal Revenue Code (from Schedule 1120 PH).....	
9. Tax from recomputing prior year investment credit (attach statement).....	
10. Total tax (sum of lines 7, 8 and 9). Enter here and on line 31, page 1.....	532,914.24

H. Date incorporated 1944

- I. (1) Did the corporation at the end of the taxable year own directly or indirectly 50 percent or more of the voting stock of a domestic corporation?..... Yes No
- (2) Did any corporation, individual, partnership, trust, or association at the end of the taxable year own directly or indirectly 50 percent or more of the corporation's voting stock?..... Yes No (For rules of attribution, see section 267 (c).)
- If the answer to (1) or (2) is "Yes," attach separate schedule showing:
- (a) name, address, and employer identification no.;
 - (b) percentage owned;
 - (c) date acquired; and
 - (d) the District Director's office in which the income tax return of such organization for the last taxable year was filed.
- If the answer to (1) above is "Yes," include the income (or loss) from line 30, page 1, Form 1120 of such corporation for the taxable year ending with or within your taxable year.
- If the answer to (2) above is "Yes," include (a) the amount of cash or stock dividends paid to such individual or organization and (b) identify form of organization.
- J. Were Forms 1096 and 1099 filed for the calendar year 1963 in connection with:
- Taxable dividends..... Yes No
 - Other payments..... Yes No
- K. Did you have any contracts or subcontracts subject to the Renegotiation Act of 1951..... Yes No
- If "Yes," see Inst. K. Enter amount here

- L. Did you at any time during the year own directly or indirectly any stock of a foreign corporation?..... Yes No If "Yes," attach statement as required by Instruction N.
- M. Amount of income (or deficit) for: 1960.. 8,205
1961.. (950,435) 1962.. 1,593,661
- N. If a cooperative association, check type:
- (1) farmers' purchasing or marketing; (2) consumers', or (3) other.
- O. Did you claim a deduction for expenses connected with: (If answer to any question is "Yes," check applicable boxes within that question.)
- (1) A hunting lodge , working ranch or farm , fishing camp , resort property , pleasure boat or yacht , or other similar facility ? (Other than where the operation of the facility was the principal business.) Yes No
 - (2) The leasing, renting, or ownership of a hotel room or suite , apartment , or other dwelling , which was used by customers or employees or members of their families? (Other than use by employees while in business travel status.) Yes No
 - (3) The attendance of your employees' families at conventions or business meetings? Yes No
 - (4) Vacations for employees or members of their families? (Other than vacation pay reported on Form W-2.) Yes No
- P. Refer to instructions and state the:
Principal business activity air transportation
Principal product or service

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Form 1120 (1963)

Schedule L.—BALANCE SHEETS. (See Instructions)

ASSETS	Beginning of taxable year		End of taxable year	
	(A) Amount	(B) Total	(C) Amount	(D) Total
1. Cash.....				
2. Notes and accounts receivable.....				
(a) Less: Reserve for bad debts.....				
3. Inventories.....				
4. Investments in Government obligations.....				
5. Other current assets (attach schedule).....				
6. Loans to stockholders.....				
7. Other investments (attach schedule).....				
8. Buildings and other fixed depreciable assets.....				
(a) Less: Accumulated amortization and depreciation.....				
9. Depletable assets.....				
(a) Less: Accumulated depletion.....				
10. Land (net of any amortization).....				
11. Intangible assets (amortizable only).....				
(a) Less: Accumulated amortization.....				
12. Other assets (attach schedule).....				
13. Total assets.....				
LIABILITIES AND CAPITAL				
14. Accounts payable.....				
15. Mortgages, notes, and bonds payable in less than 1 year.....				
16. Other current liabilities (attach schedule).....				
17. Loans from stockholders.....				
18. Mortgages, notes, and bonds payable in 1 year or more.....				
19. Other liabilities (attach schedule).....				
20. Capital stock: (a) Preferred stock.....				
(b) Common stock.....				
21. Paid-in or capital surplus (attach reconciliation).....				
22. Surplus reserve (attach schedule).....				
23. Earned surplus and undivided profits.....				
24. Total liabilities and capital.....				

ENTRIES MADE BELOW MUST BE IDENTIFIED BY ACCOUNT

Schedule M-1.—RECONCILIATION OF INCOME PER BOOKS WITH INCOME PER RETURN

1. Net income per books.....		7. Income recorded on books this year not included in this return (itemize).....	
2. Federal income tax.....			
3. Excess of capital losses over capital gains.....			
4. Taxable income not recorded on books this year (itemize).....			
5. Expenses recorded on books this year not deducted in this return (itemize).....			
6. Total of lines 1 through 5.....		9. Total of lines 7 and 8.....	
		10. Income (line 28, page 1)—line 6 less 9.....	

Schedule M-2.—ANALYSIS OF EARNED SURPLUS AND UNDIVIDED PROFITS PER BOOKS (line 23, page 4)

1. Balance at beginning of year.....		5. Distributions: (a) Cash.....	
2. Net income per books.....		(b) Stock.....	
3. Other increases (itemize).....		(c) Property.....	
		6. Other decreases (itemize).....	
4. Total of lines 1, 2, and 3.....		7. Total of lines 5 and 6.....	
		8. Balance end of year (line 4 less 7).....	

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CIVIL AERONAUTICS BOARD
Washington 25, D. C.

In Reply Refer To: B-15-68

OCT 28, 1964

AIR MAIL

Mr. Hal N. Carr
President
North Central Airlines, Inc.
6201 - 34th Avenue South
Minneapolis, Minnesota 55450

Dear Mr. Carr:

RE: Profit-Sharing, Calendar Year 1962,
Docket 12004

The Field Audits Division of the Civil Aeronautics Board has completed its audit of North Central Airlines, Inc. and has submitted its findings for the calendar year 1962 under the class rate. Upon consideration of these findings, and the CAB Form T-88 report submitted by the carrier, the earnings subject to refund pursuant to the provisions of the Local Service Class Subsidy Rate, Docket 12004, Order E-16485, as amended, have been tentatively determined by this office to be \$601,539, an increase of \$292,528 above the refund of \$309,011 as computed by North Central Airlines. Accordingly, an indicated refund of subsidy in the amount of \$601,539 is due from the carrier.

Before further action is taken, however, we want the carrier to have an opportunity to review the facts upon which we have relied in reaching the above tentative amount of profit-sharing. Accordingly, there are transmitted herewith the following CAB Form T-88 attachments.

No. 1 - Schedule A. This schedule reflects the adjusted 1962 profit-sharing computation resulting from the revenue, expense, income tax and investment adjustments made in the following attachments.

No. 2 - Schedule B. The revisions on this schedule consist of the correction of prior years findings reflected thereon, the expense adjustments per revised Schedule C - Attachment No. 3, and the adjusted income taxes per revised Schedule R - Attachment No. 6.

Mr. Hal N. Carr (2)

No. 3 - Schedule C. As revised herein, this schedule shows an increase of \$120,026 in excess of the adjustments reported by North Central. This increase is explained in detail on pages 2 through 4 of this attachment.

No. 4 - Schedule E. This schedule combines the carrier's original filing with the September 15, 1964 adjustments reported on schedules FF through LL.

No. 5 - Schedule M. This schedule has been adjusted as a result of your September 15, 1964 submission of Schedules FF through LL.

No. 6 - Schedule R. This schedule reflects adjusted 1962 income taxes.

No. 7 - Schedule V-1. This schedule summarizes the adjustments brought forward from Schedule V-2.

No. 8 - Schedule V-2. This schedule is as submitted by the carrier.

No. 9 - Schedule W. The details for adjustments are provided in the explanatory notes.

A copy of this letter and the attachments will be placed in Docket 12004 for public reference together with any reply by the carrier regarding this matter.

We plan to finalize the foregoing promptly. However, if you have any objections, they will be considered if they — together with supporting data — are sent to us within 15 days from the date of this letter.

Sincerely yours,

/s/ John B. Russell
Chief, Office of Administration

Attachments

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ATTACHMENT NO 1

CAB Form T-80
(1-14)CLASS RATE PROFIT SHARING SCHEDULE
PROFIT SHARING COMPUTATION

Carrier NORTH CENTRAL AIRLINES INC Year ended DECEMBER 31 1962

	Step I	Step II	Step III	Step IV	Step V
1. Income after tax, before profit sharing, per Schedule B	1,167,663	1,167,663	1,167,663	1,167,663	
2. Percent of investment (1 + 8)	16.61%	16.92%	16.94%	16.94%	
<u>Investment</u>					
3. Debt (Schedule W)	5,010,567	5,010,567	5,010,567	5,010,567	
4. Preferred equity (Schedule W)					
5. Common equity (Schedule W)	2,020,933	2,020,933	2,020,933	2,020,933	
6. Adjustment to common equity (50% of line 29)	-131,771	-138,775	-139,280		
7. Common equity adjusted	1,889,162	1,882,158	1,881,653		
8. Total investment	7,031,500	6,899,729	6,892,725	6,892,220	
<u>Return Element</u>					
9. Debt (5.50% x Line 3)	275,581	275,581	275,581	275,581	
10. Preferred equity (7.50% x Line 4)					
11. Common equity (21.35% x Line 7)	431,469	403,336	401,841	401,733	
12. Return element	707,050	678,917	677,422	677,314	
13. Percent of investment (12 + 8)	10.06%	9.84%	9.83%	9.83%	
14. Return at 12.75 percent	896,516				
15. Return at 9.00 percent	632,835				
16. Return at 3¢ per mile					
17. "D" return element *	707,050	678,917	677,422	677,314	
18. Earnings deficiency (1 - 17)					
<u>Profit Sharing</u>					
19. Profit to "D"	707,050	678,917	677,422	677,314	
20. "D" to 15 percent	347,675	356,042	356,487	356,519	
21. Over 15 percent	112,938	132,704	133,754	133,830	
22. Total	1,167,663	1,167,663	1,167,663	1,167,663	
<u>Carrier Share</u>					
23. Profit to "D" (100% x Line 19)	707,050	678,917	677,422	677,314	
24. "D" to 15% (50% x Line 20)	173,837	178,021	178,243	178,259	
25. Over 15% (25% x Line 21)	28,234	33,176	33,438	33,457	
26. Net profit to carrier	909,121	890,114	889,103	889,030	
<u>Government's Share</u>					
27. "D" to 15% (50% x Line 20)	178,838	178,021	178,244	178,260	
28. Over 15% (75% x Line 21)	84,704	99,528	100,316	100,373	
29. Government share before tax reduction	263,542	277,549	278,560	278,633	
30. Tax reduction ??				322,906	
31. Total to be refunded				601,539	

- * Higher of 12, 15 or 16, provided that the computed return (Line 12) does not exceed an amount equivalent to 12.75 percent of recognized investment.

- ** Show derivation of composite tax rate.

WISCONSIN
MINNESOTA
NORTH DAKOTA
IOWA

TAX RATE	ALLOCATION	%
7%	25.55	179
10.23%	1.73	151
6%	3.13	19
3%	.46	21
		3.50
		94.52%
		100.00%
		53.63%

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INTERLINE PROFIT SHARING STATEMENT

CAB Form T-40
(11-61)CLASS RATE PROFIT SHARING SCHEDULE
SUMMARY INCOME STATEMENTCarrier, CENTER CENTRAL AIRLINES INC Year ended DECEMBER 31, 1962

1. Reported operating profit or loss, per Form 41			1,490,710
2. Adjustment for subsidy revenue			
a) Formula subsidy	8,641,757		315,146
b) Reported per Form 41	8,526,611		209,029
3. Adjustments per Schedule C			14,61
4. Nonoperating income per Schedule Q			
5. Special income per Form 41			
<u>Adjustments:</u>			
a) Retrospective-subsidy	21		
b) Special income debits			
c) Special income credits-other			
6. Adjusted income before income taxes			1,975,630
7. Adjusted income taxes per Schedule R			805,167
8. Adjusted net income after taxes, before profit sharing			1,167,663
<u>2) CARRIER'S ADJUSTMENTS OF 1961 FINDINGS:</u>			
1. #49,428 - TO REDUCE 1962 REVENUES BY INTERLINE PAYABLE ADJUSTMENT EFFECTED IN 1962 BUT INCLUDED IN 1961 INCOME FOR PROFIT SHARING			
2. 3,768 TO INCREASE 1962 EXPENSE FOR NORTH CENTRAL'S PARTIAL CANCELLATION ACTION EFFECTED IN 1962 RE DEFERRED COSTS CHARGED TO OPERATING EXPENSES IN 1961			
<u># 53,196</u>	TOTAL		

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[181] 27TH INVEST INC.

CA- Form T-88
(11-61)

PAGE 1 OF 4

CLASS RATE PROFIT SHARING SCHEDULE
OPERATING REVENUES AND EXPENSES ADJUSTMENTSCarrier NorthCarolina Airlines, Inc.Year ended December 31, 1967

Reference	Revenues	
III A 1	1. Inconsistent reporting	
III A 3	2. Nontransport or affiliate (See Schedule D).	
	Total	
III B 1	Expenses	
	1. Inconsistent reporting	21 21990
III B 3a	2. Prohibited expenses <i>ITEMS FROM Prior RATE CASES</i> <i>b1</i>	51 652
III B 3b	3. Fines, etc.	
III B 3c	4. Financing costs	51 12350
III B 3d	5. Lobbying costs	
III B 3e	6. Compensation over \$25,000.	91 37210
III B 3f	7. Payments in excess of goods or services	
III B 3g	8. Bonuses	
III B 3h	9. Nonallowable dues	el 500
III B 3i	10. Nonallowable accruals	
III B 3j	11. Amortization of E & D (Details in Schedule V-1) <i>SEE REVISED SCH. V-1</i>	22 113
III B 3k	12. Witness fees	
III B 3l	13. Charitable contributions	d1 550
III B 3m	14. Life insurance premiums	
III B 3n	15.a. Nontransport or affiliate expense (See Schedule D)	
III B 3n	b. Expense not reasonably related to air service	f1 720
III B 4a	16. Affiliate expenses in excess of cost	
III B 4b	17. Unreasonable non-arm's length, etc., expenses	
III B 4c	18. Sale and lease-back	
III B 5	19. Depreciation in excess of allowable (Details in Schedule E) <i>SEE REVISED SCH. E</i>	11 430
III B 5a	20. Maintenance to conform to built-in overhaul (Details in Schedule N)	
	Total	11 430
	Net Adjustment	209 023

EXPLANATORY DETAILS - SCHEDULE C

a. INCONSISTENT REPORTING.

1. PAYMENTS FOR VARIOUS LEGAL FEES,
SPECIAL SERVICES, PERSONNEL EXPENSE
REPORTS, AND OTHER EXPENDITURES WHICH
WERE IDENTIFIED AS ROUTE DEVELOPMENT
^{AND}
COSTS, WERE CHARGED TO OPERATING
EXPENSES.

\$ 16,244

2. TO EXTEND THE AMORTIZATION
PERIOD FOR RENTAL PREPAYMENTS
AT O'HARE AIRPORT TO 20 YEARS. 24,127

3. TO ADJUST FOR LEGAL FEES AND
EXPENSES RELATING TO AIRCRAFT
ACQUISITION CHARGED DIRECTLY TO
OPERATING EXPENSES.

1,609\$ 41,960

TOTAL

b. ITEMS FROM PRIOR RATE CASES

1. DISALLOWANCE OF CAPITALIZED
BURDEN ON DC-3 AIRFRAME OVERHAUL
AMORTIZED TO 1962 MAINTENANCE
EXPENSE.

\$ 46,036

2. EXCESS RESERVE PROVISION ON
DC-3 EXPENDABLE SPARE PARTS.

56,162
\$ 51,652

TOTAL

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GITA-LINE T-7 NO. 3

SF 3 OF -1

EXPLANATORY DETAILS - SCHEDULE C

C FINANCING COSTS

1. PAYMENTS OF EXPENSE REPORTS
OF A.E.A. MUELLER IDENTIFIED AS
FINANCING COSTS WERE CHARGED
TO OPERATING EXPENSES. \$ 1,472
2. DEPRECIATION EXPENSE FOR 1962
WAS CHARGED WITH AMORTIZATION OF
CAPITALIZED FINANCING COSTS. 882
3. DISALLOWANCE OF ONE-HALF OF
THE SALARY AND EXPENSE REIMBURSEMENTS
OF R.W. HUGGETT. 7985
\$ 10,339
- TOTAL

d. CHARITABLE CONTRIBUTIONS

1. DONATIONS CHARGED TO OPERATING
EXPENSES AND NOT REPORTED ON
T-88 SCHEDULE C. \$ 550

e. NONALLOWABLE DUES

1. DUES AND CONTRIBUTIONS PAID TO
THE MINNEAPOLIS CLUB WERE CHARGED
TO OPERATING EXPENSES AND NOT REPORTED
ON T-88 SCHEDULE C. \$ 500

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ATTACHMENT NO 3
EXPLANATORY DETAILS - SCHEDULE C

EXPLANATORY DETAILS - SCHEDULE C

f. EXPENSE NOT REASONABLY RELATED TO AIR
SERVICE

1.Disallowance of one-third of
the expenses of A.L. WHEELER - Vice
President and Counsel. Out-of-pocket
expenses comprised \$14,400 of the
total amount \$ 78.39

g. As submitted by CARRIER.

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ATTACHMENT NO. 4

CLASS RATE PROFIT SHARING SCHEDULE SUMMARY FLIGHT EQUIPMENT DEPRECIATION ADJUSTMENT BY QUARTERS					
Carrier	Year ended <u>December 31, 1962</u>				
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Year 1961
<u>Reported depreciation expense</u>					
Account No.					
1601	\$ 23,295	\$ 21,361	\$ 19,650	\$ 17,366	\$ 192,181 1/
" 1602					102,443 2/
" 1603					
" 1604					
" 1605					
" 1607					30,422 3/
" 1608					
Total flight equipment	\$ 23,295	\$ 21,361	\$ 19,650	\$ 17,366	\$ 217,093
<u>Computed depreciation expense</u>					
Account No.					
1601	\$ 18,162	\$ 16,530	\$ 15,275	\$ 14,341	\$ 64,033 1/
" 1602					104,636 2/
" 1603					
" 1604					
" 1606					
" 1607					23,115 3/
" 1608					
Total flight equipment.....	\$ 18,162	\$ 16,530	\$ 15,275	\$ 14,341	\$ 192,253
<u>Adjustment</u>					
Account No. 1601	\$ 5,133	\$ 4,831	\$ 4,184	\$ 3,525	\$ 17,673 1/
" 1602					(143) 2/
" 1603					
" 1604					
" 1606					
" 1607					1309 3/
" 1608					
Total flight equipment	\$ 5,133	\$ 4,831	\$ 4,184	\$ 10,691	\$ 22,039
Cumulative To Schd. W.					

NOTES:

1.1 AS REPORTED BY CARRIER ON INITIAL SUBMISSION
OF 1962 T-88 SCHEDULES

2.1 AS REPORTED BY CARRIER ON SUPPLEMENTAL FILING OF GROUP DEPRECIATION SCHEDULES.

S.S. Form T-86
(1-61)

CLASS RATE PROFIT, SHARING SCHEDULE

Carrier North Central Airlines Inc.ADJUSTMENT TO REPORTED INVESTMENT IN FLIGHT EQUIPMENT
AS OF 12/31/61Year ended DECEMBER 31, 1961

Flight Equipment	Reported					Reclassified				
	Cost	Reserve for Depreciation	Airworthiness Reserve	Net Book Value (1-2-3)	Undepreciated Cost	Residual Value	Balloon Overhaul Residual	Computed Uncovered Freight	Net Book Value (4-5-6-7-8)	Adjustment (9)
DC-3 AIRCRAFTS	\$3,034,461	\$2,015,629	\$23,759	\$965,073	\$109,963	\$246,672		\$5,193,69	\$1,935,1	\$1,223,11
DC-3-400 + Comets	561,983	492,356	-	69,632	109,659	56,190		165,353	(96,26)	
CV-240	377,316	57,459	-	309,857	182,373	56,597		238,970	72,537	
DC-4 Airframe Repairs	100,027	107,772	-	32,255	27,494	14,003		41,497	(6,12)	
DC-3 Airframe Repairs	36,425	29,238	-	7,187	6,424	3,710		10,124	(29,83)	

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ATTACH IX, EXHIBIT K-05

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ATTACHMENT TO 106

GAR Form T-6B
(11-61)TAX RATE PROFIT SHARING SCHEDULE
INCOME TAX ADJUSTMENT - SUMMARYCarrier Airway Charter Services Inc.Year ended DECEMBER 31 1962

	Federal	State	Total
1. Pro forma adjusted income for tax purposes, before income tax and profit sharing. (Include gross formula subsidy).....	\$ 1,523,091		
2. Tax related to 1 above per pro forma tax returns submitted herewith	21 760,847	31 47,320	
3. <u>Adjustments:</u>			
a) Taxes applicable to capital gains on flight equipment. See Schedule T			
b; Taxes applicable to non-transport ventures. See Schedule 3.			
c) Tax effect of retroactive subsidy. See Schedule U.			
d) Total adjustment			
4. Adjusted taxes	\$ 760,847	\$ 47,320	\$ 808,167

NOTES

1- TAXABLE INCOME FOR AMENDED RETURN ADD 1962 SUBSIDY HELD BACK IN 1963
ADD 1962 PROFIT SHARING Est. 1,035,412
172,533
31,149
\$ 1,523,091

2- DEPENDENTS 52% OF LINE 1 LESS a) \$ 5,500 AND b) INVESTMENT CREDIT
OF \$ 25,660.

3- ESTIMATED REVISED STATE TAX RETURNS NOT RECEIVED. ARRIVED
AT BY APPLYING SAME RATIO OF TAXABLE INCOME TO STATE TAX
(\$ 1,524,654 : \$ 47,362 IN)
\$ 1,523,091 : 47,320
TO BE REvised Subsequently when state Returns ARE Received

Tax income per 1 above

Adjusted Form 41 income per
Schedule B, line 6

Difference

Schedule R

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CAB : 47-88
(1-64)

CLASS RATE PROFIT-SHARING SCHEDULE

DEVELOPMENTAL AND OPERATING COSTS

Carrier NORTH CENTRAL AIRLINES, INC.Year ended DECEMBER 31 1962

	As at 1/1/62	Quarter ended:			
		3/31/62	6/30/62	9/30/62	12/31/62
<u>Investment Adjustment-Private</u>					
1. To exclude non-recognized balance in account 1830 at beginning of year (Per V-2).....	- 167,874	- 167,874	- 163,544	- 159,338	- 165,572
2. To exclude non-recognized additions to account 1830 (Per V-2).....	XX	- 0 -	- 124	- 10,564	- 5,757
3. Reported amortization of account 1830 charged to account 6133.....	XX	- 0 -	- 0 -	- 0 -	- 0 -
4. Reported amortization of non-recognized amounts in account 1830 charged to account 7074.1.....	XX	+ 4,330	+ 4,330	+ 4,330	+ 7,128
5. Cumulative adjustment (prorate).....	- 167,874	- 163,544	- 159,338	- 165,572	- 164,201
<u>Operating Expense and Equity Investment Adjustments</u>					
6. Reported amortization of amounts in account 1830 charged to account 7074.1.....	XX	22,443	22,443	22,443	25,241
7. Computed amortization per V-2.....	XX	12,113	12,113	12,113	12,113
8. Expense adjustment.....	XX	10,330	10,330	10,330	13,128
9. Equity investment adjustment (Line 8 - Line 4).....	XX	6,000	6,000	6,000	6,000
(Cumulative).....		6,000	12,000	18,000	24,000
11. To offset against equity the Detroit City Airport amortization, consistent with the investment adjustment, Schedule V-1					

Schedule V-1

Schedule V-1

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= T-104116-LUT-407

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IAS Form T-23
(11-61)

CLASS RATE PROFIT SHARING SCHEDULE

DEVELOPMENTAL AND PREOPERATING COSTS

Carrier: NORTH CENTRAL AIRLINES, INC.

Year ended DECEMBER 31, 1962

Docket Number	Extension and Development As of 12/31/61		Additions During 1962 by Quarters				Remaining Quarters at 12/31/61	Amortization Per Quarter (Lower of 1 or 2)	Computed Amortization of Amount Recognized Quarters Ended					
	Reported	Recognized	3/31/62	6/30/62	9/30/62	12/31/62			9	10	11	12	13	
	1	2	3	4	5	6	7	8						
KC1	100								DENIED	8/14/62				
7050	100								DISMISSED	8/14/62				
7141	11,262	11,262												
7617	5820	5,820												
7454	44,348	20,799												
4251	162,072	43,412												
CV INTEGRATION	52,259	52,259												
9891	4,056													
10905	1,436													
11158	20													
110422	19,161													
12583	630													
12849	162													
13391														
13743														
9767														
Use it or lose it														
	301,126	133,552	--	124	10,564	5,757			12,113	12,113	12,113	12,113	16,453	

Schedule V-2

Schedule V-2

CIA Form 113
(1-64)Carrier *National Carriers, Inc.*CLASS RATE PROFIT SAVING SCHEDULE
INVESTMENTYear ended *Dec. 31, 1962*

	Balance Sheet As At:					Average Investment			
	12/62	3/31/62	6/30/62	9/30/62	12/31/62	Long-term Debt	Preferred Equity	Common Equity	Total
Qualified investment per Form 41									
Long-term debt.....	3,363,977	3,363,007	3,293,038	3,952,936	5,135,117	4,156,262			4,156,262
Deferred eq.									
Non-current equity.....	2,205,511	1,921,542	2,533,563	2,802,713	2,843,415				2,423,720
Total.....	5,568,488	5,284,549	6,826,601	6,761,651	7,953,532	4,156,262			2,423,720
Adjustments									
Identified as debt or equity:									
as capital due beyond three months.....	8,104,101	71,362	1024,345	1,179,358	1,019,171	-65,192			
in current discount and expense on cost.....	-59,321	-56,231	-52,930	-51,734	-49,882	-52,912			
Equipment-replacement-fund-gains.....	130,041	16,050	16,050	7,214	-	-			
Capital stock expense.....				-3,002	-3,002				
Reserves applied to charges to operating expenses.....	-303,868	-303,868	-303,868	-303,968	-303,968				-303,868
Out-of-period subsidy.....	-1,511	6,000	12,000	18,000	24,000				-9,592
Amortization of develop. and proper.-per schedule V.....				12,976	12,976				12,976
Accrued W adjustment.....	12,976	12,976	12,976	12,976	12,976				12,976
Accrued or expense-per schedule E.....				5,133	9,964	14,118	24,839		10,476
Maintenance expense-per schedule E.....					162,001	142,667			58,334
Cumulative diff. between gross and reported subsidy after tax.....	-242,701	-221,155	-197,607	-174,253	-139,820				-196,013
Inconsistent reporting.....									
Total.....						5,067,543	71,224		2,013,957
Debt-equity ratio.....									28.76%
High end or debt-equity ratios:									
Operating property.....									
Invest. in affil. or nontrans. activity-per schedule D.....									-11,375
Cash value of life insurance.....	-10,934	-10,934	-10,934	-10,934	-10,934				
Equipment replacement funds other than gain.....									
Equipment purchase deposits.....									
Certified organization expense.....									-1,000
Special funds.....	-1,000	-1,000	-1,000	-1,000	-1,000				
Working capital in excess of 3 months' expenses.....									
Construction work in progress.....									-163,372
Overrecognition of develop. and proper.-per schedule V-1.....	-167,874	-163,541	-159,533	-165,571	-159,201				96,313
Inconsistent reporting.....	96,000	96,000	96,000	96,000	96,000				
Total pro-rated adjustments.....						-16,976			-23,024
Total adjusted investment.....						501,0567			2020,923

(a) SEE ACCOMPANYING NOTES.

Schedule W

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North Central Airlines, Inc.
EXPLANATORY NOTES. SCHEDULE W

	1/31/61	3/31/62	6/30/62	9/30/62	12/31/62	1/31/63
To Equity:						
(a) To adjust for foreign accrual of income taxes.						
Reported income taxes	\$170,000				\$675,761	\$106,720
(less) Tax on Gross Formula Subsidy (See N below)	127,616				172,479	37,512
TOTAL INCOME TAXES PER LINE 2, SCHEDULE R	\$42,387				-808,167	-153,314
	\$-116,911					
Line 15. THE EFFECT OF THE COMPOSITE TAX RATE ON THE DIFFERENCE BETWEEN GROSS AND REPORTED SUBSIDY						
CUMULATIVE GROSS FORMULA SUBSIDY DIFFERENCE						
Less: Tax at composite rate of 54.73% (Schedule A)					\$357,854	\$315,146
					-195,653	-172,479
Net Adjustment					\$162,001	\$142,667
(a) TRANSFER TO EQUITY THE ADJUSTMENT OF \$120,000 ESTIMATE OF WILLOW RUN DETROIT CITY OPERATION	\$96,000	\$96,000	\$96,000	\$96,000	\$96,000	\$96,000
(b) DISALLOWED AMORTIZATION OF RENTAL PREPAYMENT AT O'HARE AIRPORT	6551	13,102	19,653	26,210	13,103	7,166
(c) Nonallowable depreciation on DC-3 equipment	140	544	544	1,609	538	
(d) Nonallowable legal fees and expenses related to aircraft acquisition.						
(e) CAPITALIZED BURDEN ON DC-3 AIRFRAME OVERHAUL BROUGHT FORWARD FROM THE PRIOR RATE CASE AND RECOGNIZED ON A CASH BASIS IN 1962.	-146,701	-134,619	-122,367	-110,701	-100,665	-12,511
(f) FRESS RESERVE PROVISION ON DC-3 EXTRAMABLE SPARE PARTS.	1,104	2,805	4,212	5,616	2,208	
(g) De minimis costs charged to expense.	1369	2,406	6,039	16,284	2,339	
Total	\$-242,101	\$-221,155	\$-197,507	\$-174,233	\$-130,220	\$-24,642
To Release:						
Non-Tax item \$36,000 AS REPORTED FOR ADJUSTMENT BY THE BOARD OF ACCOUNTS ON SCHEDULE V-1.	\$96,000	\$96,000	\$96,000	\$96,000	\$96,000	\$96,000

NORTH CENTRAL AIRLINES, INC.
EXPLANATORY NOTES SCHEDULE W

1962

	12/31/61	3/31/62	6/30/62	9/30/62	12/31/62	PERCENT
Line 5: Total amount reported by the carrier	- 45542	- 12633	- 39724	- 51704	- 47582	- 15.13
Financing costs capitalized	- 14090	- 13648	- 13206	--	-	- 13.75
TOTAL	- 59632	- 56281	- 52930	- 51704	- 53352	- 53.91%
Line 7:						
(a) Aeroline payables two years old or older	1 49428	1 7414	1 7414	1 7414	1 - -	1 1129
(b) To capitalize items charged to expense	8636	8636	8636	--	--	539.9
TOTAL	1 58064	1 10050	1 16050	1 7414	1 - -	1 17137
Line 9:						
(a) To reduce common equity by 1961 profit sharing	1 303868	1 303868	1 - 303868	1 - 303868	1 - 303868	1 - 303868

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NORTH CENTRAL AIRLINES, INC.
General Offices: 6201 Thirty-Fourth Avenue So.
Minneapolis, Minn. 55450

November 4, 1964

Mr. John B. Russell, Chief
Office of Administration
Civil Aeronautics Board
Washington, D. C. 20428

Re: Profit Sharing, Calendar Year 1962
Docket 12004 (B-15-68)

Dear Mr. Russell:

Thank you for your letter of October 28 to our President, Mr. H. N. Carr, regarding North Central's profit sharing for 1962. Mr. Carr has asked me to reply as financial matters are a function of my department.

I have reviewed your letter and the attached T88 schedules. It appears that there are a number of items in the schedules that will require a thorough analysis before we are able to answer your letter. This is especially true in connection with the investment adjustments in Schedule W.

Mr. Daniel F. May, our Treasurer, is responsible for all matters pertaining to profit sharing under the Class Rate. He has been out of the office this week due to illness, but we expect him back the first part of next week for a few days. However, he is scheduled to be on vacation the following week and will be gone until after Thanksgiving.

In view of Mr. May's absence and also the substantial amount of money involved in the matter, we request a 30-day extension of time in which to reply to your letter and file revised T88 schedules. Your consideration of our request will be sincerely appreciated.

Very truly yours,

NORTH CENTRAL AIRLINES,
INC.

/s/ Bernard Sweet
Vice President-Finance

BS:ph

cc: Mr. H. N. Carr
Mr. D. F. May

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NORTH CENTRAL AIRLINES, INC.
General Offices: 6201 Thirty-Fourth Avenue So.
Minneapolis, Minn. 55450

November 5, 1964

Mr. John Russell, Chief
Office of Administration
Civil Aeronautics Board
Washington, D. C. 20428

Dear Mr. Russell:

I am enclosing copies of our 1962 and 1963 amended Corporation
Income Tax Returns for the State of North Dakota.

I would appreciate it if you would attach these to our T88 schedules for these years.

Very truly yours,

NORTH CENTRAL AIRLINES,
INC.

/s/ Daniel F. May
Treasurer

DFM/jd
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CIVIL AERONAUTICS BOARD
Washington 25, D. C.

In Reply Refer to: B-68

NOV 13, 1964

AIR MAIL

Mr. Bernard Sweet
Vice President-Finance
North Central Airlines, Inc.
6201 Thirty-Fourth Avenue So.
Minneapolis, Minnesota 55450

Dear Mr. Sweet:

This is in response to your letter of November 4, 1964, requesting a 30-day extension of time in which to reply to our letter of October 28, 1964, regarding North Central's profit-sharing for 1962.

Your Treasurer, Mr. May, and Mr. Donaldson of the Board's Subsidy Division discussed this matter on the telephone. It was agreed that, in view of Mr. May's familiarity with the various exceptions taken in our letter, North Central would submit, for presentation to the Board, written objections to the staff's final position as to profit-sharing for 1962 by November 23, 1964. Accordingly, we will delay further action on this matter until that date.

Sincerely yours,

/s/ John B. Russell
Chief, Office of Administration

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NORTH CENTRAL AIRLINES, INC.
General Offices: 6201 Thirty-Fourth Avenue So.
Minneapolis, Minn. 55450

November 20, 1964

Mr. John Russell, Chief
Office of Administration
Civil Aeronautics Board
Washington, D. C. 20428

Dear Mr. Russell:

Thank you for your letter of November 13 granting us the extension of time in which to reply to your October 28 letter to our president, Mr. H. N. Carr, regarding North Central's 1962 profit sharing.

In your letter of October 28 you asked that we review your field audit staff's tentative findings and submit our comments. However, in your November 13 letter you stated that during Mr. Donaldson's telephone conversation with Mr. May, "It was agreed that in view of Mr. May's familiarity with the exceptions taken in our letter, North Central would submit for presentation to the Board written objections to the staff's final position."

I have reviewed this matter with Mr. May and he has advised me that he did not agree that we were replying to your "final position." Rather it was his understanding that your staff would review our comments and then if there were still areas of disagreement, we would have an opportunity to discuss them with members of your staff in an informal conference before your final position was reached. We are, therefore, submitting the following comments in response to your letter of October 28 regarding our 1962 profit sharing.

1. Workmen's Compensation Premium Adjustment

In your 1961 profit sharing return, schedule C, line 1, you reduced 1961 expenses by \$3,696 for a return premium which was booked in the 1410 account.

In July of 1962 we reclassified this item from prepaid insurance to the Workmen's Compensation accrual account. In December, 1962 we adjusted the accrual account to reflect the estimated liability as of 12/31/62. This resulted in an expense reduction of \$3,696 in 1962.

The recorded liability as of 12/31/62 was as follows:

North Dakota	\$ 507.95
Ohio	154.50
All other states	\$36,480.12

The first two items were paid in January, 1963. The last item was paid during 1962 on a deposit basis. At the year end, account 1410

reflected the deposit premium of \$52,183. The insurance company advised us that we could anticipate a refund in the amount of \$15,703. We, therefore, adjusted the accrual account to reflect the net estimated liability of \$36,480.

The Workmen's Compensation policy is a three year policy with a profit sharing feature. The final year of this policy was 1963. As of this date, we do not have the final premium computation for the full three year period. However, from preliminary reports it appears that the estimated liability which was booked during this three year period may be a little understated. We hope to have the final premium computation for the total policy period before the end of this year.

2. Financing Costs

Your schedule C proposes a disallowance of 50% of the salary and expense reimbursements to R. W. Huggett as financing costs. Mr. Huggett may have spent some of his time in work that might be construed as being related to financing in connection with our 1963 debenture sale. Since his primary duties involved public relations, community relations, publicity, employee relations and administrative functions that would normally be associated with an assistant to the Chairman of the Board of Directors; and furthermore since North Central has one of the lowest general and administrative costs in the local airline industry, we do not believe that a disallowance is justified.

However, in an effort to resolve this matter that is now two years old, we would agree to a disallowance of 15% of Mr. Huggett's salary and expenses.

3. Costs Not Reasonably Related to Air Service

In your 1961 audit your auditors took the position that some of Mr. Wheeler's expenses were not adequately documented. In 1962 when this finding was presented to us, we asked Mr. Wheeler to furnish us with the documentation for 1962 which the auditors deemed necessary. Mr. Wheeler did this and all the information was available during the audit of the 1962 records in 1963. The \$14,400 was completely explained and documented. This amount was paid as direct reimbursement of expenses incurred in maintaining his office. We also obtained documentation for the other reimbursed expenses. We have complied with the request of the audit staff and we can see no basis for making this disallowance in 1962.

4. Investment Credit

On Schedule R, you proposed a reduction in the tax computation to allow for investment credit of \$25,660.

We are of the opinion that this is not in accordance with the intent of Congress, it is contrary to law and we cannot, therefore, accept the finding proposed in your letter.

In addition to the items discussed above, the following adjustments should be made to the T88 schedule for 1962 as per our Mr. Daniel May's telephone conversation with your Mr. Ken Donaldson.

Schedule B

1. Carriers adjustment of 1961 findings.

Items capitalized in 1962 charged to expense in 1961 (see schedule W, line 7b) \$8,636.

2. Schedule Q Income

Eliminate \$2,701 for interest income which was earned on deposit for O'Hare hangar in 1961. This investment was disallowed in 1961.

The interest income on this investment was not recorded until 1962 as per audit finding. Line 4 of schedule B should be \$11,440.

Schedule R

Revised schedule attached reflecting state income tax per revised returns and elimination of investment credit of \$25,660.

Schedule W

1. Line 3, fourth quarter should include an additional \$10,818 which is the deferred income credit portion of the investment tax credit for 1962.
2. Line 6, should include disallowed depreciation expense on capitalized financing costs (see schedule C, line 4, item 2). This adjustment in the amount of \$1,469 should be made to last two balance sheets.
3. Line 7, should include the \$3,696 Workmen's Compensation adjustment made in 1961. This item was taken into income in December, 1962.
4. Line 9, should be \$198,909. This is the \$303,868 equity adjustment on the final 1961 T88, less the booked equity adjustment of \$104,959 per our original T88.
5. Line 10, should be adjusted to reflect the corrected tax element on line 15 and adjusted schedule R tax.
6. Line 15, composite tax rate should be 53.68% instead of 54.73%.

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We would appreciate your consideration of our comments and if you are not in agreement with our position, we request an informal conference with your staff to discuss the matter further.

Very truly yours,
NORTH CENTRAL AIRLINES, INC.

/s/ Bernard Sweet
Vice President-Finance

cc: Mr. Daniel F. May
cc: Lear, Scoutt & Rasenberger

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NORTH CENTRAL AIRLINES, INC.
General Offices: 6201 Thirty-Fourth Avenue So.
Minneapolis, Minn. 55450

November 20, 1964

Mr. John Russell, Chief
Office of Administration
Civil Aeronautics Board
Washington, D. C. 20428

Dear Mr. Russell:

Attached is our schedule R, which we omitted as an enclosure to
Mr. Sweets letter of today.

Very truly yours,
NORTH CENTRAL AIRLINES, INC.

/s/ Daniel F. May
Treasurer

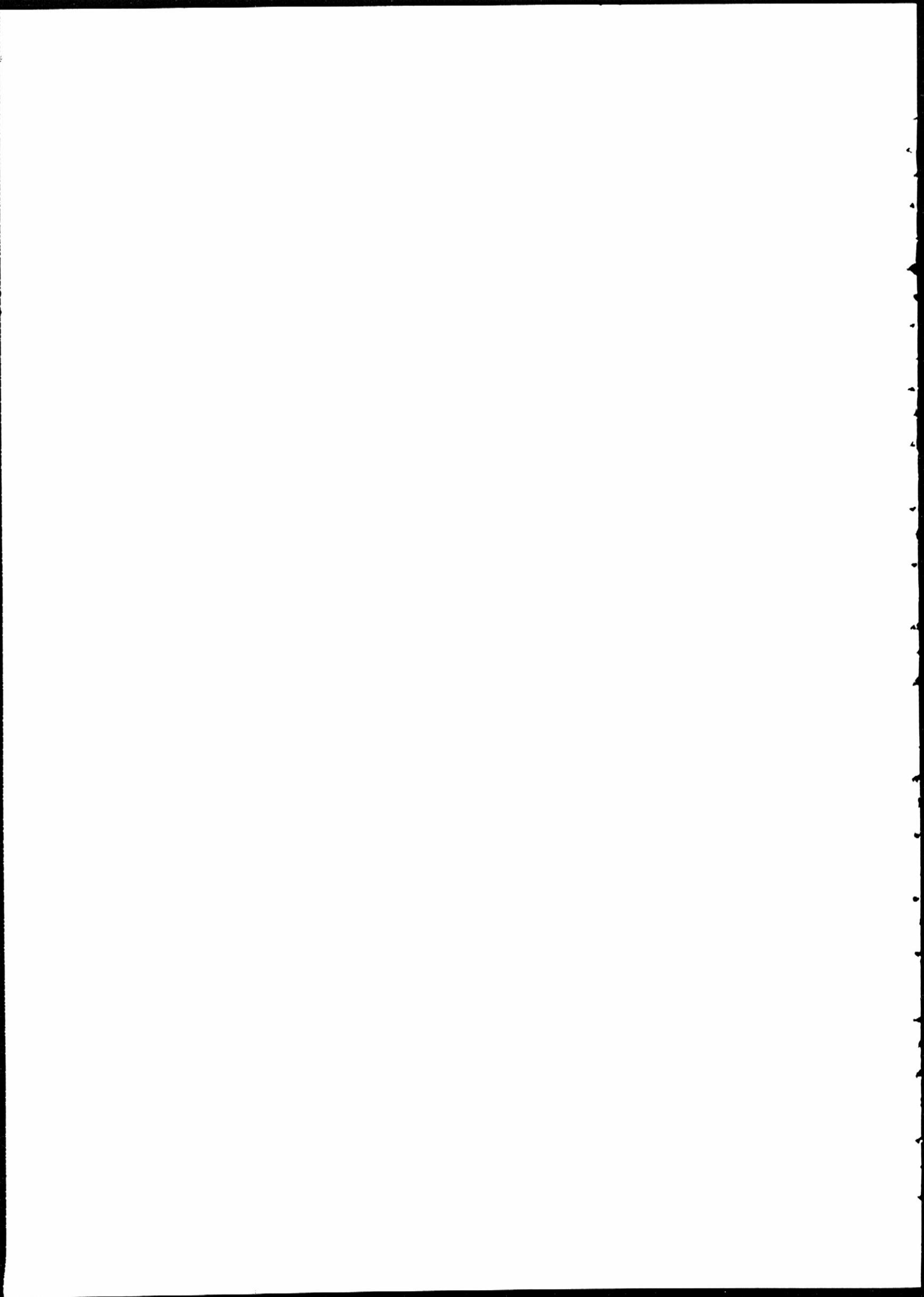
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CAB Form T-88
(1-64)CAB RATE PROFIT SHARING SCHEDULE
INC'S TAX ADJUSTMENT - SUMMARYCarrier North Central Airlines, Inc.

Year ended December 31, 1962

	Federal	State	Total
1. Actual or adjusted income for tax purposes, before income tax and profit sharing. (Include gross formula subsidy).....	1,505,845	607,194	
2. Tax related to 1 above	777,539	47,556	
3. <u>Adjustments:</u>			
a) Taxes applicable to capital gains on flight equipment. See Schedule T			
b) Taxes applicable to non-transport ventures. See Schedule S.			
c) Tax effect of out-of-period subsidy. See Schedule U.			
d) Total adjustment	777,539	47,556	825,095
4. Adjusted taxes	777,539	47,556	825,095
Federal Taxable Income per amended return	1,035,412		
Add. Mail Subsidy held back in 1962	172,533		
Add. 1962 Profit Sharing Estimate	315,146		
	1,523,091		
Add. State Income Taxes as amended	30,310		
Less - State Income Taxes computed (see below)	-47,556		
	1,505,845		

State	STATE TAX COMPUTATION					
	Wisconsin	Minnesota	No. Dakota	Iowa	Canada	Total
Federal Taxable Income	1,523,091	1,523,091	1,523,091	1,523,091		
Add: State Income Taxes	18,152	12,158	30,310		100	
Contributions Not Allow.	595	595			595	
Less: Federal Taxes Deductable	= 105,146	= 227,850	= 227,850	= 227,850		
	1,436,692	1,307,994	1,325,551	1,295,936		
Allocation	25.55%	14.73%	3.13%	.46%		43.87%
Income Subject to Tax	367,075	192,668	41,490	5,961		607,194
Less Contributions and Special Credits		1,095				
		191,573				
Rate	7% \$195	10.23%	6% \$260	3%	50	47,556
	25,500	19,598	2,229	179		



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Attachment I

Law Offices
LEAR, SCOUTT & RASENBERGER
Brawner Building
Washington, D. C. 20006

December 2, 1964

Mr. John Russell, Chief
Office of Administration
Civil Aeronautics Board
Washington, D. C. 20428

Re: North Central Airlines, Inc.
1962 Profit Sharing

Dear Mr. Russell:

This concerns your letter of October 28, 1964, to Mr. H. N. Carr regarding North Central's 1962 profit sharing. Among the profit-sharing adjustments proposed by you was a reduction in the tax computation of North Central to delete the benefit of the investment tax credit. Mr. Sweet's letter to you of November 20, 1964, indicated that North Central is of the opinion that the adjustment described above is contrary to law. The purpose of this letter is to state North Central's objections in further detail.

As you are aware, the Revenue Act of 1962 (Public Law No. 87-834) amended section 38 of the 1954 Internal Revenue Code to provide that an investment tax credit shall be allowed in the amount established by section 46 of the Code. Under these provisions, as recently interpreted by Congress, North Central is entitled to a tax credit of \$25,660 and the Board may not reduce by this amount the sums lawfully due North Central under the class rate.

The Revenue Act of 1962 makes no exception for equipment purchased by regulated companies; nevertheless, in two agencies, the FCC and FPC staff, it was held that the investment tax credit could not be retained by regulated companies but should "flow through" to the consumer. Accordingly, in the 1964 Act (section 203(e), PL 88-272), it was made perfectly clear that it was the intent of Congress in 1962, and is still the intent of Congress, that no agency or instrumentality of the United States should take advantage of the investment tax credit in establishing the cost of the service of the taxpayer or in accomplishing a similar result.

Much debate surrounded the enactment of this clarifying amendment in 1964. From the amendment, and from the underlying legislative history, it is abundantly clear that Congress intended section 203(e) to apply to all taxpayers (including subsidized air carriers) and all agencies of the United States

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States (including the Civil Aeronautics Board). In support of this we are attaching a memorandum on the question. This memorandum was originally prepared by Mr. James M. Verner in connection with a proceeding similar to this. It well summarizes the applicable law and legislative history and North Central concurs in its reasoning and conclusions.

The Board, in its Statement of Provisional Findings and Conclusions for Class Rate III, has nevertheless concluded that, despite the provisions of the 1954 Code and the interpretative language of section 203(e) of the Revenue Act of 1964, the investment tax credit should be taken account of in determining the cost of service of local service carriers for purposes of computing "need" under section 406(b) of the Federal Aviation Act (Order E-21227, August 28, 1964). We have reviewed the reasons given by the Board for adoption of that position.

Such reasons, we submit, indicate that the Board has completely misread the intent of the law.

First, the Board suggests that:

"To infer that a statute materially alters a fundamental principle of subsidy rate regulation (the actual tax policy in this case), it must clearly appear that Congress intended such an effect" (Order E-21227, p. 34-35).

As the attached memorandum indicates, the intent of Congress could hardly have been made more clear. It is true, of course, that Congress could have specifically addressed itself to the actual tax policy of the Board or to section 406(b). However, under the principle of expressio unius est exclusio alterius, Congress could not deal with some regulatory statutes and agencies specifically without dealing with them all. In short, Congress stated its intent as fully and clearly as was possible.

We fail to understand what more the Board could have expected.

Second, the Board observed that:

"The results intended by section 203(e) for other regulated industries and nonsubsidized airlines - that is, the encouragement of development and expansion - are already provided for subsidized airlines by section 406(b) of the Federal Aviation Act. . . . If need has been otherwise met under this provision, which was designed to meet the special problems of the airline industry (particularly the subsidized airlines) for certain purposes, it can hardly be argued that the carriers 'need' the benefit of the investment tax credit for the same purposes."

In short, the Board finds that section 203(e) may be ignored because its purposes are redundant with and in conflict with those of section 406(b).

This is completely in error. The purposes of the two statutes are quite different. Congress' objective in the tax law is to provide a new and added incentive, to be applied without regard to the existence of other incentives. The objective is not the promotion of an adequate system of air transportation. It is the stimulation of the national economy. The method is to superimpose on existing tax incentives, existing public utility rates, even if now adequate, and other existing economic incentives the stimulus of this tax deduction.

The distinction between the purposes of section 203(e) and 406(b) is evidenced clearly by the legislative history. Thus, the Secretary of the Treasury told the Senate Finance Committee:

"I urge this legislation because it will make a real addition to growth consistent with the principles of a free economy; because it will provide substantial help in alleviating our balance-of-payments problem, both by substantially increasing the relative attractiveness of domestic as compared with foreign investment and by helping to improve the competitive position of American industry in markets at home and abroad; and because, far from adding to the forces responsible for alternative recessions and recoveries, it will be of major assistance in strengthening our present recovery and enabling us to attain a higher rate of growth and sustained full employment. Early action will resolve uncertainty or hesitancy and begin at once a strong and lasting incentive for modernization of the productive facilities of our national economy." U.S. Code Cong. and Admin. Laws, 87th Cong., 2nd Sess., p. 3313.

This objective is echoed by the report of the Senate Committee which described the need for investment tax credit as follows:

"The objective of the investment credit is to encourage modernization and expansion of the Nation's productive facilities and thereby improve the economic potential of the country, with a resultant increase in job opportunities and betterment of our competitive position in the world economy." Ibid. p. 3314.

This sentiment is echoed in the legislative history underlying section 203(e) of the Revenue Act of 1964. In describing that amendment the Congress stated:

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"It is your Committee's intent that the financial assistance represented by the credit should itself be used for new investment, thereby further advancing the economy." Ibid. 88th Cong., 2nd Sess., p. A-34

The Civil Aeronautics Board has not been charged with the responsibility for stimulating the national economy in general. It is true that, in the process of fixing adequate rates under section 406(b), the Board may contribute to that objective. But Congress has found that more is required. It has called for a blanket economic stimulant. It has not authorized government agencies to decide whether existing incentives, including subsidy programs, are alone sufficient to provide that stimulant. The Board may entertain whatever doubts it has about the wisdom of adding this economic incentive to those provided by section 406(b). But for larger purposes, Congress has found differently and it has specifically forbidden the Board, or any other agency, from applying existing law so as to negate the added incentive of the investment tax credit.

In light of these considerations, and the matters set forth in the attachment hereto, North Central Airlines strongly objects to the position taken by the staff in this matter and we urge that the position

of the staff and the apparent position of the Board be revised in conformity with the applicable law.

Sincerely,

/s/ Raymond J. Rasenberger

Attorney for North Central Airlines, Inc.

RJR: mm

Attachments

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June 23, 1964

MEMORANDUM:

QUESTION: Does the Board have the authority to treat the investment credit granted by the Internal Revenue Code as a reduction of income taxes in its determination of profit-sharing in connection with the Class Rate?

ANSWER: No. Section 203(e) of the Revenue Act of 1964, P.L. 88-272 prevents the Civil Aeronautics Board from treating the investment tax credit allowed a carrier as a reduction in taxes for the purpose of computing subsidy.

I The Statute

Section 203(e) of the Revenue Act of 1964, P.L. 88-272 provides:

"TREATMENT OF INVESTMENT CREDIT BY FEDERAL REGULATORY AGENCIES.— It was the intent of the Congress in providing an investment credit under section 38 of the Internal Revenue Code of 1954, and it is the intent of the Congress in repealing the reduction in basis required by section 48(g) of such Code, to provide an incentive for modernization and growth of private industry (including that portion thereof which is regulated). Accordingly, Congress does not intend that any agency or instrumentality of the United States having jurisdiction with respect to a taxpayer shall, without the consent of the taxpayer, use —

(1) in the case of public utility property (as defined in section 46(c)(3)(B) of the Internal Revenue Code of 1954), more than a proportionate part (determined with reference to the average useful life of the property with respect to which the credit was allowed) of the credit against tax allowed for any taxable year by section 38 of such Code, or
(2) in the case of any other property, any credit against tax allowed by section 38 of such Code,
to reduce such taxpayer's Federal income taxes for the purpose of establishing the cost of service of the taxpayer or to accomplish a similar result by any other method." (emphasis added)

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Applicability. Section 203(e) is declarative of the intent of Congress in providing the tax credit in 1962.

Section 203(e) is applicable to the treatment of the investment credit by federal regulatory agencies for all periods since the credit was adopted in 1962. It was the avowed purpose of the sponsors of section 203(e) to render certain the intent of the Congress in its initial providing of the credit. Accounting for periods prior to the adoption of section 203(e) must therefore reflect this intent.

The debates on a motion by Senator Proxmire to strike section 203(e) clearly demonstrate that it is declarative of the 1962 enactment. Senator Long, of Louisiana, the floor manager of the bill, explained that Congress in 1962 intended that federal regulatory agencies should not have the power to require the benefit of the tax credit to "flow through," and that the regulated industries should be allowed to retain the credit.

The legislative history as made on the floor of the Senate by the late Senator Kerr of Oklahoma, who was the Senator in charge of the bill, suggested, when the bill was initially considered, that it was the intention of the Senate that the tax credit be passed through. When the matter went to conference, the House and Senate conferees reached an agreement. The understanding between Senator Kerr and the House managers was that the tax credit would not be passed through. 110 Cong.

Rec. 1977-78 (1964)

This interpretation was insisted upon by the House conferees and was accepted by the Senate conferees. Two of the Senate conferees on the 1962 measure supported Senator Long's explanation of the legislative

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history of the investment credit. See remarks of Senator Anderson, 110 Cong. Rec. 1980 (1964); remarks of Senator Carlson, 110 Cong. Rec. 1989-90 (1964).

After the credit was adopted, a hot dispute arose in the regulatory agencies as to the actual intent of Congress. Finally, in closely divided decisions, the Federal Power Commission (by a 3 to 2 vote) and the Federal Communications Commission (by a 4 to 3 vote) held that it was the intent of Congress that the benefit of the tax credit should flow through to the consumer and should not be retained by the regulated utility. See 110 Cong. Rec. 1980 (1964).

Section 203(e) was proposed to correct this misreading of Congressional intent, which was attributed by Senator Long to the uncertainty arising from Senator Kerr's statements on the floor when the credit was initially debated. 110 Cong. Rec. 1978 (1964). Senator Simpson was less charitable and viewed the action of these agencies as a defiance of the clear mandate of Congress. Id. at 1987-88. In any

event all were agreed that the purpose of the 1964 provision was to make clear beyond doubt the meaning of the 1962 enactment.

The Senate Report on the Revenue Act also addresses itself to this question, indicating that section 203(e) was intended to correct the erroneous administrative reading of the legislative intent behind the tax credit. The committee reports which it cites are the reports on the original proposal for the investment credit which culminated in the 1962 enactment. The manager who is quoted is Senator Kerr:

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"A fourth modification in the investment credit relates to the treatment of the credit by regulatory bodies. Both the House and Senate committee reports on the investment credit, as well as the statement of the managers on the part of the House with respect to the conference (and the floor statement on the Senate with respect to the conference report) state that the purpose of the investment credit was to stimulate investment by reducing the net cost of acquiring depreciable assets. This is shown by the following quotations. First, in the report of the Committee on Ways and Means of the House on that bill:

'The investment credit will stimulate investments because—as a direct offset against the tax otherwise payable—it will reduce the cost of acquiring depreciable assets. This reduced cost will stimulate additional investment as it increases the expected return from their use. The investment credit will also encourage investment because it increases the funds available for investment. * * * '

"In the report of your committee on that bill it was stated:

'The investment credit will stimulate investment, first by reducing the net cost of acquiring depreciable

assets, which in turn increases the rate of return after taxes arising from their acquisition. * * *

'The objective of the credit is to reduce the net cost of acquiring new equipment; this will have the effect of increasing earnings of new facilities over their productive lives and increasing the profitability of productive investment. It is your committee's intent that the financial assistance represented by the credit should itself be used for new investment, thereby further advancing the economy.'

"Again, in the statement of the managers on the part of the House with respect to the conference committee, and also in the floor statement of the manager of the bill in the Senate, it was stated:

'It is the understanding of the conferees on the part of both the House and Senate that the purpose of the credit for investment in certain depreciable property, in the case of both regulated and nonregulated industries, is to encourage modernization and expansion of the Nation's productive facilities and to improve its economic potential by reducing the net cost of acquiring new equipment, thereby increasing the earnings of new facilities over their productive lives.'

"Despite the statements cited above, the Federal Communications Commission has indicated that it is its policy that any benefits from the investment credit made available by the Revenue Act of 1962 should 'flow through' immediately to the customers. In addition, the staff of the Federal Power Commission has recommended the same position. This is

clearly contrary to the intent of Congress in enacting this provision and as a result this bill contains a provision to the effect that it was and is not Congress' intention that the Federal regulatory agencies require the benefit of the investment credit to 'flow through' in this manner." (emphasis added) S. Rep. No. 830, 88th Cong. 2d Sess. 42-43 (1964).

The same point was reiterated:

"(c)(iii) TREATMENT OF INVESTMENT CREDIT BY FEDERAL REGULATORY AGENCIES — Another investment credit provision in the bills makes it clear that it was the intent of Congress in providing an investment credit in 1962, and it is the intent of Congress this year in repealing the reduction in basis required [by the 1962 Act] with respect to investment credit assets, to provide an incentive for the modernization and growth of private industry, including regulated industries." (emphasis added) Id. at 44.

Thus, the unequivocal intention of the Congress in incorporating section 203(e) in the Revenue Act of 1964 was to clarify beyond doubt the legislative intent of the 1962 act creating the investment credit. Section 203(e), therefore, governs all treatment of the investment credit by federal regulatory agencies irrespective of whether the equipment investments giving rise to the credit were made before or after the adoption of the 1964 Act. If a tax credit is allowable under the Internal Revenue Code, it is protected from federal agency action.

II Section 203(e) prevents the inclusion of tax credit in the computation of subsidy.

Section 203(e), in terms, states its purpose as guaranteeing "incentive[s] for modernization and growth of private industry (including that

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portion thereof which is regulated)." The purpose is attained by denying a federal regulatory agency the power to (1) "reduce such taxpayer's Federal income taxes for the purpose of establishing the cost of service of the taxpayer" or (2) "to accomplish a similar result by any other method."

A. Reducing Taxes to Establish Cost.

The meaning of section 203(e) can be determined only in the light of its purpose. The legislative history of the Revenue Act of 1964 makes abundantly clear that the purpose of Congress was to guarantee to regulated industries the incentives for modernization and expansion sought to be attained by the investment credit, and to deny to any federal agency the power to vitiate these incentives by treating the tax credit as a reduction in taxes. Most of the legislative history revolved around the question of rate-making proceedings, but this was because of the FPC and FCC decisions discussed supra. The Committee Reports and floor debates demonstrate that the House Ways and Means Committee, the Senate Finance Committee, and the supporters of sec. 203(e) on the floor were not concerned with rates qua rates, but with preserving the incentives for plant investment that were the basis for section 203's repeal of the 1962 requirement of a 7 per cent reduction in basis of the subject property. Hence, any agency action which treats the investment credit as a reduction in taxes (or conversely as an increase in income, which is the same thing) and as a result denies the benefit of the tax credit is

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barred by sec. 203(e). The CAB proposes to do just this by its employment of the tax credit to reduce taxes for the purpose of establishing subsidy.

This is a plain violation of the express language of section 203(e).

Section 203(e) does not say that this treatment of the tax credit is forbidden only in rate-making proceedings. It says that under no circumstances can an agency use the tax credit to reduce taxes for the purpose of establishing the cost of service.

The legislative history makes it quite clear that the CAB was among the agencies in the minds of the Congress when it dealt with this bill. But neither the proponents nor the opponents of section 203(e) felt that the Board would deny the benefit of the credit to airlines under its jurisdiction.

Opponent Javits expressed concern that airlines would be required to pass through the credit and asked of Senator Proxmire, author of the motion to strike:

Mr. Javits: What about the ones who regulate the aircraft companies, and so forth, does the Senator from Wisconsin have information [as to whether they would require a flow-through] from them?

Mr. Proxmire: I have none from the Civil Aeronautics Board, although I understand that this would be a fairly academic question at the present time, because I think that most of those companies are not earning in excess of a fair return. 110 Cong. Rec.

1972 (1964).

Why was the CAB position academic in Senator Proxmire's view? He considered it academic because he, and every other opponent of section 203(e) assumed that the agencies would allow marginal companies to retain the benefit of the credit. They were directing their fire at

electric long lines and pipelines, not the struggling transportation industry. The debates make clear that their goal was not to require

a pass through in all cases but only to avoid a Congressional mandate against a pass through in any case.

Thus Senator Proxmire, an opponent of section 203(e), said with respect to railroads:

"... many of these industries are not earning a fair return, in some cases. Under the circumstances, they should receive full value as stock holders of the investment credit with no pass through. (emphasis added)

110 Cong. Rec. 1974 (1964).

Senators Pell and Kuchel took the same position. Id. at 1974, 1971 Senator Magnuson, also an opponent of 203(e) as written said:

"... I cannot assume that in every case the Commission would require that the tax credit be passed on. Perhaps the finances of a particular utility company would not justify a requirement that the credit be passed on at this particular time. (emphasis added)

Id. at 1958-59.

And the same point was made in a colloquy between Senators Douglas and Proxmire, both opponents of sec. 203(e):

Mr. Douglas: Is it not true that possibly in the case of some railroads — I am not certain that it would hold true for every railroad — the Interstate Commerce Commission may find that the rates at present are inadequate to enable them to earn a fair return on the fair value, and that in those cases the Interstate Commerce Commission may say that the benefit should not be passed on.

Mr. Proxmire: Yes.

"As the Senator from Illinois knows, many railroads are not doing well financially. In those cases,

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the benefit would not be passed on. The railroads would always be entitled to a fair return." (emphasis added). 110 Cong. Rec. 1970-71 (1964)

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In short even the opponents of sec. 203(e) did not advocate the denial of the retention of this credit by marginal companies. They assumed that the regulatory agencies would allow such companies to derive the benefit of the credit. They clearly did not foresee that the Board would deny the incentives for expansion and modernization to precisely those operators most in need of it.

The essence of what the Board proposes to do is made clear in a little parable related by Senator Douglas during the course of the debates:

"**Mr. Douglas:** Suppose there were two men, one of whom ate only two meals a day and the other ate four meals a day, and we gave the equivalent of a meal a day in tax credit. The regulatory body says, 'The man who has only two meals a day deserves it so that he can get three meals a day. He gets his three meals a day through the investment credit.'

"Are we then going to say, because we give an extra meal to an underfed man, that we must 'super-stuff a man who is already getting four meals.' "

110 Cong. Rec. 1974 (1964).

It might be noted that the Congress of the United States responded in the affirmative by adopting sec. 203(e). Both men get that extra meal. What the Board proposes by recognizing that the tax credit may not be counted in ratemaking, while asserting that it may be included in subsidy would accomplish an end to which both the proponents and the opponents of sec. 203(e) were clearly opposed.

The Board says, "We will 'superstuff' the man who is already getting four meals, (the non-subsidized carriers) but we are not going to give that extra meal to the underfed man. He still has to get along on two meals a day."

It is clear that the foregoing will be the result if the Board determines to treat the investment credit as a reduction of taxes and then applies its actual tax policy. A proposed rule, issued by the Board on October 2, 1963, if adopted would provide that 100 percent of the credit be taken into income in the case of subsidized carriers as compared to 48% for unsubsidized carriers. This confirmed, accounting-wise, the disposition of the Board to require, in the case of subsidized carriers that the tax credit "pass through" to the Government. However, the Board advised Senator Albert Gore that Board action on the proposed rule would be deferred pending disposition of House Resolution 8363.^{1/} The action now contemplated by the Staff and Board runs counter to the action taken by the Congress on H.R. 8363, which resulted in section 203(e).

B. Accomplish a Similar result by any other method.

The inclusion of the investment credit in fixing subsidy is even more clearly contrary to Congressional intent when viewed in the light of the provision of sec. 203(e) that prohibits Federal regulatory agencies from "accomplish[ing] a similar result by any other method." The "similar result" is the denial of the incentives of the tax credit; it is not adopting a particular form of rate-making. It was not the Commerce Committee of the Congress that presented the section; it was the House

1/ A letter reprinted at 110 Cong. Rec. 1984-85 (1964).

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Ways and Means Committee and the Senate Finance Committee. These bodies are concerned with tax writing, and in this particular case, they were concerned with preserving the incentive they sought to grant by the 1962 tax regulation.

Their purpose was to prevent federal regulatory agencies from denying the benefits of the tax credit. Those benefits are as effectively denied by a reduction in subsidy as by a reduction in rates. In either case, management incentives are sapped. In the latter, the credit flows through to the consumer; in the former it flows through to the government. This difference is immaterial since it is the fact of the flow-through which destroys the incentive, not the ultimate destination. The method used to provide these incentives was, after all, a decrease in government revenues, in effect a subsidy. If the CAB can recall to the Federal Treasury what the Internal Revenue Service has given up, the subsidized airline industry alone of all American business is excluded from the incentives provided by the investment credit. The compelling need Congress saw for inducing plant modernization and expansion to strengthen our economy will, as to subsidized airlines, remain unmet. Yet subsidized industries are precisely those most in need of these incentives.

The Report of the Senate Finance Committee makes crystal clear that sec. 203(e) was intended as a protection for airlines as well as other businesses and that any device which would include the tax credit in income so as to deny to the taxpayer the ability to retain the credit was forbidden.

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"(c)(iii) TREATMENT OF INVESTMENT CREDIT
BY FEDERAL REGULATORY AGENCIES — Another
investment credit provision in the bill makes it clear

that it was the intent of Congress in providing an investment credit in 1962, and that it is the intent of Congress this year in repealing the reduction in basis required with respect to investment credit assets, to provide an incentive for the modernization and growth of private industry, including regulated industries.

"The bill also provides restrictions for Federal regulatory agencies in the case of other regulated companies — such as natural gas pipelines, railroads, airlines, truck and bus operators, and other types of public utility investment in qualified property. It provides that Federal regulatory agencies are not, without the taxpayer's consent, for purposes of establishing the cost of service of the taxpayer, to treat any investment credit allowed him as reducing his Federal income taxes. Nor are the agencies to accomplish a similar result by any other method.

"As indicated above in the case of the public utility property Congress is merely directing the Federal regulatory agencies not to 'flow' the benefits of the investment credit 'through' to the customers over any period shorter than the useful lives of the property involved.

In the case of the other property Congress is directing the Federal regulatory agencies not to 'flow' this benefit 'through' at any time." (emphasis added). S. Rep. No. 830, 88th Cong. 2nd Sess. 44-45 (1964).

The goal was that the taxpayer should retain the credit. Congress, in effect, said in 1962, "If you spend your money in what is, by our lights, an economically desirable way, we will give you a 7 percent tax break." They made this even more clear in 1964 by repealing the requirement that the taxpayer write down the basis of the newly acquired

property by 7 per cent. The result was an outright gift, or subsidy if you will, rewarding those taxpayers who expend corporate funds for expansion or modernization. Any federal regulatory action that denies that reward, and therefore that incentive, was the object of section 203(e). That was the result forbidden, and action, by whatever name, that accomplishes a similar result is violative of the Act.

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As Senator Magnuson said:

"It seems to me that if we are to give a tax benefit to a corporation — and I do not care which corporation it is — it is useless to say, 'We will give you a tax benefit, but you cannot have it; you must pass it on.' We might as well let things stand the way they are."

110 Cong. Rec. 1956 (1964).

Senator Proxmire responded that a pass-through reducing rates would increase consumer demand and therefore justify additional equipment expenditure and so attain the goal of inducing expansion and modernization. This is a tenable position, although it was rejected by the Congress in favor of the view that the best incentive would be to allow the companies to retain the credit. But even Senator Proxmire's position has no relevance to the Board's proposed action. For a pass-through in the form of a subsidy reduction will not adhere to the benefit of the consumer. It will not increase demand. It will remove an important incentive for equipment purchases and negate the purpose of the tax credit. It is precisely this end that the Congress sought to forbid.

The goals of section 203(e) were expressed in a colloquy between Senators Long and Douglas:

"Mr. LONG of Louisiana. My understanding is that [a pass-through is allowed] is true of all of the

3-percent utilities, which include the local utilities, the electric light companies, and the telephone companies.

"Mr. DOUGLAS. But it is not true to the 7-percent companies, which include all forms of transportation — including the railroads and the airlines — and especially the gas and oil pipelines, and possibly also the long telephone lines, or any company, whether it gets the 3- or 7-percent credit which is under Federal regulation.

"Mr. LONG of Louisiana. My understanding is that the 3-percent utilities did expect to pass it through, and always did take that position.

"Mr. DOUGLAS. But under the present law, if they are federally regulated, they are prohibited from passing it on.

"Mr. LONG of Louisiana. I believe the Senator will discover even in the House language that there is a difference between the two.

"With regard to the 7-percent facilities, which includes the transportation industries —

"Mr. DOUGLAS. And the gas and oil pipelines.

"Mr. LONG of Louisiana. Those are transportation industries, and are included.

"Mr. DOUGLAS. Yes.

"Mr. LONG of Louisiana. With respect to the transportation industries including the bargelines, airlines, and trucklines, the position taken by the House as of today is that the 3-percent utilities never expected to keep it, but expected to pass it through, and proposed to do so. But the 7-percent utilities have a different proposal.

"Those industries are competitive with one another, and the companies within each of those industries are also competitive with each other. The trucklines are competitive with other trucklines; the bargelines are competitive with other bargelines; the railroads are competitive with other railroads; and shipping lines are competitive with other shipping lines; and all of them are competitive with each other. So the House takes the position that inasmuch as those are competitive both with one another and with carriers of other industries, they should be permitted the same incentive that is available to other competitive industries.

"The Senator from Illinois does not have to agree with that; but I hope he understands that is the rationale of the House version of the bill." (emphasis added).
Cong. Rec. 1293 (1964).

Senator Douglas did agree to the extent that he felt that marginal carriers should be allowed to retain the credit, Id. at 1294-95, and see Part II A, supra. He was concerned with the pipelines and electric longlines because he felt that they did not need the credit to stimulate investment. The Congress rejected that view and voted to let all seven percent companies retain the credit.

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III No Valid Distinction As Between Board and Other Agencies.

Two arguments which might be advanced to support the Board's position are: (1) The Congress has not amended Section 406 of the Federal Aviation Act by the Revenue Act of 1964; and (2) consideration of the tax credit as revenue (or as reduced taxes) so as to decrease allowable subsidy is not included in the proscription which is that an agency may not "reduce such taxpayer's Federal income

taxes for the purpose of establishing the cost of service of the taxpayer or to accomplish a similar result by any other method." i.e. a distinction between the fixing of mail rates and commercial rates.

The Argument that Section 406 has not been amended.

The Congress, in adopting sec. 203(e), was not engaged in a simple hortatory declaration. It clearly intended a binding amendment of all statutory ratemaking schemes. This was one basis on which the opponents of sec. 203(e) grounded their arguments. They maintained that since the provision was amendatory of all federal rate-making procedures, it should have been handled by the Commerce Committees of the Congress rather than the Ways and Means and Finance Committees. Thus Senator Proxmire, sponsor of the proposal to strike sec. 203(e) said: "It is mandatory on the Federal agencies." 110 Cong. Rec. 1955 (1964). And in response to a question as to whether 203(e) would prevent the FPC from ordering refunds of past overcharges, he said: "The provision in the bill would interfere with the power of the Federal Power Commission to reduce rates." Id. at 1958.

Senator Williams of Delaware added:

"If the section is allowed to remain in the bill, it will specifically provide that the regulatory agencies cannot under any circumstances pass through any of the benefits of the investment credit to the consumers.

That is spelled out in clear language." Ibid.

Senator Magnuson, Chairman of the Commerce Committee, protested:

"First, let me say that it seems to me it is not good policy for Congress to set up the Federal Power Commission and expect it to do a good job as between the consumers and the utilities, and give it sufficient

authority for that purpose, and then include in a tax bill a provision which would prohibit the Commission from doing certain necessary or desirable things.

Ibid.

"Furthermore, I do not believe that the Finance Committee should determine that policy; I do not think the Finance Committee should, after Congress has directed that a tax credit be given, take the position that Congress should instruct the Commission exactly what should be done with the tax credit." Id. at 1959.

To which Senator Proxmire added:

"I point out that unless this amendment [striking sec. 203(e)] is enacted into law, the pending tax bill will include a wholly unprecedented Congressional dictation to regulatory bodies. . ." Ibid.

Mr. Church indicated the sweeping nature of sec. 203(e):

"The Senator's amendment is addressed to a single provision in the bill which interferes with the kind of discretion the regulatory Commissions have always had. . . [Is] not this a matter of public policy that properly should be considered by the legislative committee which is charged with such responsibility?"

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Mr. Proxmire:

"The Senator is correct. That is what my amendment would do. It would eliminate from the bill the provision in question. It would eliminate from the bill a matter which I believe comes under the jurisdiction of the Commerce committee, and provides that this shall be a tax-cut bill, and only a tax-cut bill. Id. at 1967.

And Senator McGovern:

"I am in agreement that we should not in a tax bill, attempt to legislate the manner in which the utilities should be regulated. . . .

"Even if we were to assume — which I do not think we should assume — that it might be desirable to change the powers of the regulatory commissions, should that be done in a tax bill, or should it be done after careful consideration and review by the Commerce Committee which properly has jurisdiction over this field."

Mr. Proxmire:

"We should not. . . Id. at 1968.

Senator Kuchel:

"It has been recognized by many that sec. 203(e) is not a tax proposal at all — It is a regulatory proposal, and thus it should not be in a tax bill. Id. at 1971.

The proponents of sec. 203(e), in response, did not deny that the provision was a general amendment of all rate-making statutes, and a binding limitation on the discretion of the agencies. Their position was that since the purpose of the restriction was to enforce tax policy, and prevent depredations on tax benefits by federal agencies it was properly handled by the tax-writing committees. As Senator Long said:

"So far as Federal commissions are concerned, they are created by Congress and are regarded as an arm of Congress. We establish them and say how they are to do business. We prescribe the general standards that are to be used in determining what a fair return is.

"When we vote a tax cut, a big question is raised. So far as ordinary competitive industry is concerned,

industry that is not subject to regulation, it is clear that we intended it to get the benefit of the tax cut which is an investment credit.

"But Congress also voted a similar tax cut for regulated industries. Are we to leave the Commissions in doubt as to whether that credit should be recouped from the carrier or the utility? Should we not have the responsibility of instructing them and saying, 'Yes; we intended that they should have this tax cut as an incentive to modernize and expand?'"

Mr. Saltonstall:

"In other words, the Senator from Louisiana is saying that . . . the CAB, with respect to airlines, should not have any discretion with relation to the tax investment credit?"

Mr. Long of Louisiana:

"It seems to me that we should tell them, one way or the other." Id. at 1979.

And Senator Morton said:

"I cannot see anything wrong with having Congress tell the regulatory agencies what Congress meant 2 years ago when it passed the 1962 bill." Id. at 1995.

Mail Rate v. Commercial Rate Fixing The Board's attempt to distinguish between subsidy and commercial ratemaking is contrary to the Federal Aviation Act of 1958. In litigation under its predecessor, the Civil Aeronautics Act of 1938, the Board took the position that the same procedural rules were applicable equally to mail, passenger and property rates under the Act. Trans-continental & Western Air, Inc. v. Civil Aeronautics Board, 336 U.S. 601, 608 (1949) (dissent of Justice Jackson). The Board maintained that sections 406 and

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1002 were both governed by the general rules of public utility regulation, and the Supreme Court agreed, finding that Congress so intended.

TWA maintained that the element of "need" or subsidy in the fixing of sec. 406 rates transmuted the proceeding to something more than a simple rate-making one. The Court said:

"The language of sec. 406(b) which empowers the Board to 'fix and determine' after notice and hearing 'the fair and reasonable rates of compensation' for the transportation of mail by aircraft reads like a typical public utility ratemaking authority. Both subdivision (a) and (b) of sec. 406, to be sure, reflect some characteristics of rate-making which are peculiar to air carriers . . ." Id. at 604.

With respect to the subsidy element, the Court said that the inclusion of

". . . such a standard has its counterparts in other legislation dealing with ratemaking." Ibid.

The Court concluded that

"The language of the Act does not suggest that Congress intended to break with these traditions of ratemaking."

Id. at 605.

A comparison of the language of secs. 406(b) and 1002(e) compels the same conclusion. They are virtually identical:

Sec. 406(b):

"In fixing and determining fair and reasonable rates of compensation under this section, the Board, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers may fix different rates for different air carriers or classes of air carriers, and different classes of service. In deter-

mining the rate in each case, the Board shall take into consideration, among other factors, (1) the condition that such air carriers

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may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; (2) such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and (3) the need of each such air carrier (other than a supplemental air carrier) for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense." (emphasis added)

Sec. 1002(e):

"In exercising and performing its powers and duties with respect to the determination of rates for the carriage of persons or property, the Board shall take into consideration, among other factors —

- (1) The effect of such rates upon the movement of traffic;
- (2) The need in the public interest of adequate and efficient transportation of persons and property by air carriers at the lowest cost consistent with the furnishing of such service;

- (3) Such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law;
- (4) The inherent advantages of transportation by aircraft; and
- (5) The need of each air carrier for revenue sufficient to enable such air carrier, under honest, economical, and efficient management, to provide adequate and efficient air carrier service." (emphasis added)

In the light of the TWA decision and the Board's past policy, there is no warrant for the Board's attempt now to distinguish secs. 406 and 1002 for the purpose of avoiding the prohibition of sec. 203(e).

IV. CONCLUSION

The manifest legislative purpose of sec. 203(e) of the Revenue Act of 1964 was to forbid any federal regulatory agency action which would deny to companies subject to their jurisdiction the benefits of the tax credit. A Board policy of reducing Federal taxes by the amount of the credit in the determination of the subsidy flies in the face of the unequivocal statutory language and the legislative intent. Subsidized airlines alone will be denied the benefit of this provision which Congress envisioned as a public necessity to stimulate our economy.

The incongruity of such a ruling is that it was precisely these carriers that all participants in the debates on the bill agreed should retain the credit.

CRS Form T-28
(1-64)CLASS RATE PROFIT SHARING SCHEDULE
PROFIT SHARING COMPUTATION
Carrier AMERICAN AIRLINES, INC. Year ended DECEMBER 31, 1962

	Step I	Step II	Step III	Step IV	Step V
1. Income after tax, before profit sharing, per Schedule B	1,161,403	1,161,403	1,161,403	1,161,403	
2. Percent of investment (1 + 8)	16.28%	16.55%	16.55%	16.58%	
<u>Investment</u>					
3. Debt (Schedule W)	5,011,894	5,011,894	5,011,894	5,011,894	
4. Preferred equity (Schedule W)					
5. Common equity (Schedule W)	2,123,147	2,123,147	2,123,147	2,123,147	
6. Adjustment to common equity (50% of line 29)	- 119,507	- 125,128	- 125,749		
7. Common equity adjusted	2,123,147	2,093,640	1,995,019	1,994,398	
8. Total investment	7,135,041	7,015,534	7,006,913	7,006,292	
<u>Return Element</u>					
9. Debt (5.50% x Line 3)	275,654	275,654	275,654	275,654	
10. Preferred equity (7.50% x Line 4)					
11. Common equity (21.35% x Line 7)	453,292	427,777	425,937	425,804	
12. Return element	728,946	703,431	701,591	701,458	
13. Percent of investment (12 + 8)	10.22%	10.03%	10.02%	10.02%	
14. Return at 12.75 percent	909,716				
15. Return at 9.00 percent	642,154				
16. Return at 3¢ per mile					
17. "D" return element *	728,946	703,431	701,591	701,458	
18. Earnings deficiency (1 - 17)					
<u>Profit Sharing</u>					
19. Profit to "D"	728,946	703,431	701,591	701,458	
20. "D" to 15 percent	341,310	348,899	349,446	349,426	
21. Over 15 percent	91,147	109,073	110,366	110,459	
22. Total	1,161,403	1,161,403	1,161,403	1,161,403	
<u>Carrier Share</u>					
23. Profit to "D" (100% x Line 19)	728,946	703,431	701,591	701,458	
24. "D" to 15% (50% x Line 20)	170,655	174,446	174,723	174,743	
25. Over 15% (25% x Line 21)	22,787	27,268	27,591	27,615	
26. Net profit to carrier	922,388	905,148	903,905	903,816	
<u>Government's Share</u>					
27. "D" to 15% (50% x Line 20)	170,655	174,450	174,723	174,743	
28. Over 15% (75% x Line 21)	63,360	61,805	62,775	62,841	
29. Government share before tax reduction	239,015	256,255	257,498	257,587	
30. Tax reduction					
31. Total to be refunded					✓

* Higher of 12, 15 or 16, provided that the computed return (Line 12) does not exceed an amount equivalent to 12.75 percent of recognized investment.

** Show derivation of composite tax rate.

GAS Form T-38
(11-61)CLASS RATE PROFIT SHARING
SUGARY INCOME STATEMENTCarrier National Carriers Airlines, Inc. Year ended DECEMBER 31 1962

1. Reported operating profit or loss, per Form 41			\$ 1430,710
2. Adjustment for subsidy revenue			
a) Formula subsidy	3,841,757		
b) Reported per form 41	8,526,611	515,146	
3. Adjustments per Schedule C			209,029
4. Nonoperating income per Schedule Q			12,121
5. Special income per Form 41			
Adjustments:	63,158		
a) Retroactive subsidy	24		
b) Special income debits			< 65,183
c) Special income credits-other ..			
6. Adjusted income before income taxes			1,960,637
7. Adjusted income taxes per Schedule R			799,135
8. Adjusted net income after taxes, before profit sharing			1,161,402

CL CARRIER'S ADJUSTMENTS OF 1961 FINDINGS:

1. \$ 49,428 - TO REDUCE 1962 REVENUES BY INTERLINE PAYABLE ADJUSTMENT EFFECTED IN 1962 BUT INCLUDED IN 1961 INCOME FOR PROFIT-SHARING.
 2. 3,763 - TO INCREASE 1962 EXPENSE FOR PARTIAL CORRECTIVE ACTION EFFECTED IN 1962 RE: DEFERRED COSTS CHARGED TO 1961 EXPENSE.
 3. 2,636 - TO INCREASE 1962 EXPENSE FOR CORRECTIVE ACTION TAKEN IN 1962 ON CAPITALIZABLE EXPENDITURES CHARGED TO EXPENSE IN 1961.
 4. 17011 - TO REDUCE 1962 REVENUES BY INTEREST INCOME ON TREASURY NOTES EARNED IN 1961 BUT NOT BOOKED UNTIL 1962.
 5. 3,655 - TO REDUCE 1962 REVENUES FOR WORKMEN'S COMPENSATION REFUND CREDIT RECEIVED IN 1961 AND CREDITED TO INCOME IN 1962.
- # 63,158

Continued

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CAB Form T-88
(11-61)CLASS RATE PROFIT SHARING SCHEDULE
INCOME TAX ADJUSTMENT - SUMMARYCarrier Northeastern Airlines, Inc.Year ended DECEMBER 31, 1962

	Federal	State	Total
1. Pro forma adjusted income for tax purposes, before income tax and profit sharing. (Include gross formula subsidy).....	\$ 1,505,845		
2. Tax related to 1 above per pro forma tax returns submitted herewith	\$ 7,518.79	\$ 47,556	\$ 799,435
3. <u>Adjustments:</u>			
a) Taxes applicable to capital gains on flight equipment. See Schedule T			
b) Taxes applicable to non-transport ventures. See Schedule S.			
c) Tax effect of retroactive subsidy. See Schedule U.			
d) Total adjustment	\$ 751,879	\$ 47,556	\$ 799,435
4. Adjusted taxes			
NOTE-3:			
1- TAXABLE INCOME PER AMENDED RETURN 100% AIRLINE SUBSIDY HELD BACK IN 1962 400% 1962 PROFIT SHARING (ESTIMATED) ADJUSTED INCOME FOR 1962 LESS STATE INVESTMENT CREDIT 2- INVESTMENT 52% OF LINE 1 LESS \$15,000 AND 5% INVESTMENT CREDIT OF \$25,660.	\$ 1,035,412 177,533 \$15,146 \$15,230.91 30,310 \$ 17,556 \$ 1,505,845		
Tax income per 1 above			
Adjusted Form 41 income per Schedule B, line 6			
Difference			

Schedule R

CAB Form T-88

(1-64)

Carrier *United Parcel Service Inc.*CLASS RATE PROFIT SHARING SCHEDULE
INVESTMENTYear ended *Dec. 31, 1963*

		Balance Sheet As At:					Average Investment		
		1/1	3/31	6/30	9/30	12/31	Long-term Debt	Preferred Equity	Common Equity
1	<u>Reported investment per Form 41</u>						4,156,262		4,156,262
2	Long-term debt.....								
3	Preferred equity.....								
4	Common equity.....								
4	Total.....						4,156,262	2,413,724	2,413,724
	<u>Adjustments</u>								
	<u>Identified as debt or equity:</u>								
5	Notes payable due beyond three months.....	- 59,632	- 56,281	- 52,930	- 50,235	- 48,413	965,103		
6	Unamortized discount and expense on debt.....						- 53,367		
7	Equipment-replacement-fund-gains. <i>P2100, 17415</i>							20,535	
8	Capital stock expense. <i>1963, 2000000</i>	- 198,909	- 198,909	- 198,909	- 198,909	- 198,909		- 1,126	
9	Reserves accrued thru charges to operating expense. <i>1963, 2000000</i>							- 198,009	
10	Out-of-period-subsidy.....							- 17,464	
11	Amortization of develop. and preoper.-per schedule V-1.....							12,000	
12	Schedule M adjustment.....							12,976	
13	Depreciation expense-per schedule E.....							10,216	
14	Maintenance-expense-per schedule N.....							1,352	
15	Cumulative diff. between gross and reported subsidy after tax.							39,687	
16	Inconsistent reporting.....							- 1,6044	
17	Subtotal.....						5,068,094	2,146,917	7,215,0
18	Debt-equity ratio.....						70.25%	29.75%	100.0
	<u>Prorated on debt-equity ratio:</u>								
19	Nonoperating property.....								
20	Invest. in affil. or nontrans. activity-per schedule D.....								- 11,3
21	Cash value of life insurance.....								
22	Equipment replacement funds other than gain.....								
23	Equipment purchase deposit.....								
24	Capitalized organization expense.....								- 10
25	Special funds.....								
26	Working capital in excess of 3 months' expenses.....								
27	Construction work in progress.....								- 163,6
28	Nonrecognition of develop. and preoper.-per schedule V-1.....								96,0
29	Inconsistent reporting.....								
30	Total prorated adjustments.....						- 36,200	- 23,800	- 80,0
31	Total reported investment.....						5,111,314	2,122,127	7,215

Schedule W

North Central Airlines, Inc.

SCHEDULED NOTES - SCHEDULE W

1962

	12/31/61	3/31/62	6/30/62	9/30/62	12/31/62	MARINE
DEBT:						
Line 6: As reported by the carrier. Financing costs capitalized Provision as first shown in front present balance.	- 45542 - 14020 - -- Total	- 12633 - 13018 - -- - 56231	- 39124 - 13206 - -- - 56137	- 51704 - -- - 1469 - 50235	- 49392 - -- - 1469 - 18413	- 15443 - 8175 - 551 - 5367
EQUITY:						
Line 7: a) Helpline entries two years old or older b) To minimize items charged to expense. c) Vacations/internation refund of premium Total	19123 8636 3655 61710	7414 8636 3655 19705	7414 8636 3655 19705	7414 - -- - -- 11069	- -- - -- - -- - 104259	11739 5393 5199 20325
Line 9: 1961 profit-sharing (prior to closure) Less: Amount unpaid by Carrier Payments Total	- 303868 104959 - 195709	- 303868 104959 - 195709	- 303868 104959 - 195709	- 303868 104959 - 195709	- 303868 104959 - 195709	- 303868 5393 195709
Line 10: To adjust for (under) overaccrued or inc. rates Rate 1962 income tax Accrued on leased formula surcharge (See 15 column) Total income taxes incl. Line 2 Schedule K 15. INVESTMENT	176000 121319 - 192590 - 185711	.	.	.	675761 169170 - 799135 45196	106720 31053 - 161253 - 11164
Line 11: The amount of the investment in the investment account Accrued on investment account Accrued on investment account Accrued on investment account Total investment	100000 100000 100000 100000 100000	351351 132070 165463	315146 120170 149311	100000 100000 100000	100000 100000 100000	100000 100000 100000

NORTH CENTRAL AIRLINES, INC.
FEBRUARY 1962 TO MARCH 31, 1962 1%

	12/31/61	2/28/62	3/31/62	3/30/62	12/31/62	AMOUNT
EQUITY: (cont.)						
106						
(a) Reserve to equity THE UNAUTHORIZED ACCOUNT, DUE OF \$120,000 WHICH WAS WITHHELD DURING OPERATION	- 96000	- 96000	- 96000	- 96000	- 96000	- 96000
(b) Disallowed amortization of rental equipment at Office Airport	6551	13102	1953	26210	13103	
(c) No income recognition on DC-3 equipment				7166	896	
(d) Nonrecoverable lease fees and expenses related to aircraft acquisition	140	544	544	1609	503	
(e) Amortization booked on DC-3 equipment overpaid because FORWARDED FROM THE PERIOD RATE CASE AND RECOGNIZED ON A CASH BASIS IN 1962.	-146701	-131619	-122367	-110701	-100665	-122843
(f) Excess reserve provision on DC-3 due to three share parts of depreciation costs charged to expense	1404	2808	4212	5616	2803	
TOTAL	1369	1406	8039	16244	5184	
	-242701	-221155	-107507	-174253	-139320	-105041
LINE 14						
To REVERSE TO EQUITY PORTION OF INVESTMENT THE CREDIT DEFERRED IN ACCOUNT 2390.					10919	1352
Procedure:						
Line 19:						
To EXCLUDE \$96000 AS REPORTED FOR ADJUSTMENT BY NORTH CENTRAL ON SCHEDULE 4-1.	96000	96000	96000	96000	96000	96000

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D.C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D.C.
on the 11th day of January, 1965

-----:
LOCAL SERVICE CLASS SUBSIDY RATE :
(NORTH CENTRAL AIRLINES, INC., :
SUBSIDY REFUND - 1962) :
-----: Docket 12004

ORDER DETERMINING SUBSIDY REFUND

In this Order the Board has determined, pursuant to the provisions of Class Rate I,^{1/} that North Central Airlines, Inc. shall refund \$556,103 of subsidy for the calendar year 1962. In adopting Class Rate I, the Board established a class rate system for payment of subsidy to the local service carriers. Class Rate I, which was final and in effect for all thirteen local carriers — with one exception not relevant here — for calendar years 1961 and 1962, contains specific provisions, which, under certain conditions, provide for refund to the Government of a portion of the subsidy paid to the various local carriers. The amount of such refund, if any, is ascertained in each case on the basis of a profit-sharing scale set forth in the section of the class rate containing the rate formula. The detailed provisions for computing the income, expense, investment and tax elements entering into the profit-sharing or subsidy refund calculation — which calculation is required to be made for calendar years 1961 and 1962 — are contained in sections II and III of the rate formula.^{2/}

^{1/} Local Service Class Subsidy Rate Investigation, 34 C.A.B. 416, 418 (1961).

^{2/} The original class subsidy rate was replaced in revised form by Class Rate II, as of January 1, 1963 (Order E-19340, March 1, 1963, and Order E-19405, March 22, 1963) and by Class Rate III, as of July 1,

1964 (Order E-21227, August 28, 1964, and Order E-21311, September 22, 1964). The profit-sharing or subsidy refund provisions of the revised rates are substantially similar to those of the original rate formula. In addition, under the applicable formula an earnings deficiency for 1962 may be carried forward for two successive years as an offset against profits in such two years.

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To facilitate the profit-sharing and subsidy refund provided for in Class Rate I, the Board requires each local service carrier to submit a special report, Form T-88, on an annual basis.^{3/} This form and the provisions of the class rate which it effectuates are so designed that the administration of profit-sharing and subsidy refund does not involve rate-making determinations, but solely the ascertainment of the pertinent facts and the application of the provisions of the formula to those facts.^{4/}

On April 12, 1963, North Central submitted the required CAB Form T-88 in connection with the determination of the amount of profit-sharing for 1962.

In accordance with established practice, North Central's Form T-88 for calendar 1962, as amended, has been subjected to field audit by the Board's staff at the site of the carrier's operations and a staff report of the audit findings has been made to the Board. Upon review of the audit report, the carrier's Form 41 reports, the data contained in the carrier's T-88 report, and the supplemental materials developed in communications and discussions between North Central and the Board's staff, the Board has concluded that under the terms of Class Rate I North Central shall refund \$556,103 in subsidy for calendar year 1962. The Form T-88 submitted by the carrier for 1962 conforms to, and is consistent with, the requirements of Class Rate I, except in the following respects:

1. Section III A 1 of the Class Rate requires that reports of revenues be consistent with the reporting requirements of the Act and the

Board's Regulations. Pursuant to this section and in connection with the 1961 subsidy refund determination involving North Central (Order E-21319, September 23, 1964), a number of adjustments to the carrier's 1962 T-88 are required:

(a) In 1961 the carrier determined that \$49,428 of interline traffic payables were aged and not likely to become the basis of claims. In our profit-sharing order we therefore included this item in the carrier's 1961 revenues. However, the carrier did not transfer the amount to passenger revenue until 1962, and, as a result, the item has been included in its T-88 report for that year. Consistent with our prior adjustment, the \$49,428 has been eliminated from the reported 1962 revenues.

(b) An escrow deposit was excluded from the carrier's investment as a restricted fund. That deposit earned \$2,701 in interest in 1961 but this amount was not recorded until 1962. Consistent with our prior elimination of the investment, the interest income has been excluded from 1962 revenues.

^{3/} Form T-88 is entitled "Report of Earnings Subject to Profit-Sharing Pursuant to the Provisions of Local Service Class Subsidy Rate, Docket 12004, Order E-16485, As Amended."

^{4/} Since Class Rate I is final, as is true of all class rates, its provisions are not open to contest retroactively and are not in issue in determinations such as the instant one.

(c) In 1961 the carrier's T-88 was adjusted to reflect a workmen's compensation insurance premium credit but the carrier did not make the appropriate book entry until 1962. In view of our prior adjustment, \$3,655 has been eliminated from the income reported on the carrier's 1962 T-88 report.

2. Under section III B 1 of the Class Rate, expenses reported for profit-sharing must be consistent with the reporting require-

ments of the Act and the Board's accounting regulations. Pursuant to this section, the following adjustments have been made:

(a) In connection with the 1961 profit-sharing determination developmental costs in the amount of \$3,768 and expenditures in the amount of \$8,636 were eliminated from operating expenses since they should have been capitalized. In 1962 the carrier effected the necessary corrective action on its books and this is reflected in the T-88 reports. Therefore, in view of the 1961 adjustment, an appropriate modification has been made to the carrier's 1962 reported results.

(b) As of January 1, 1962, North Central began the amortization of a prepayment relating to the lease of a water reservoir and pump house facilities at O'Hare International Airport in Chicago. The period of amortization was fixed by the carrier at five years, but prepaid rent on hangar facilities at the airport is being amortized over 20 years. Since the reservoir and pump house are part of the overall airport facilities and have the same expected useful service life to the carrier, recovery of these costs should also be amortized over a 20-year period. Therefore, the reported results have been adjusted to eliminate \$24,127, representing the amount of excess amortization taken by the carrier.

(c) We have excluded from operating expenses \$1,609 for legal fees and expenses relating to the acquisition of aircraft. Under the Board's accounting regulations these expenses should have been capitalized in the appropriate property accounts, and the carrier's T-88 has been adjusted accordingly.

3. In North Central's last individual subsidy case^{5/} various disallowances were made with regard to DC-3 maintenance and obsolescence expense. In its 1962 expenses the carrier reported \$51,652 of these disallowed costs. In view of their prior nonrecognition, these expenses have been excluded for profit-sharing purposes.

4. Paragraph j of section III B 3 requires the disallowance of expenses incurred for proceedings in which the carrier is an unsuccessful

applicant for a route award. In addition, this provision also provides that expenses incurred during the prosecution of an exemption or route award be held in abeyance pending final decision of the Board. Under this provision, \$16,244 of miscellaneous developmental costs charged to operating expenses have been excluded.

^{5/} 34 C.A.B. 126 (1961).

5. Financing costs and costs related to financing are nonallowable expenses as specified in paragraph c of section III B 3. In this category we have eliminated \$10,339 from operating expenses. Of this amount \$7,985 represents half of the salary and expenses of an assistant to the chairman of the carrier's board of directors. On the basis of the audit report and information submitted by the carrier we have concluded that 50 percent of the assistant's time was devoted to matters directly related to financing, and therefore that portion of his salary and expenses has not been recognized.^{6/}

6. Paragraphs h and l of section III B 3 provide, respectively, for the disallowance of dues expensed on behalf of the carrier or any officer or director, unless such dues are for membership in business, professional, or trade organizations and for the disallowance of charitable contributions. Pursuant to these sections we have excluded \$500 and \$550, respectively.

7. A review of North Central's reported results reveals that \$7,839 of expenses of a vice-president who maintained an out-of-town office should not be recognized. A similar disallowance was made in connection with the 1961 profit-sharing determination. Contrary to the carrier's apparent position our disallowance for 1962, as well as for 1961, are not primarily based on a lack of support of the fact of the expenditures having been made, but on our findings that the expenses did

not reasonably relate to the air transport services of North Central. Accordingly, pursuant to paragraph n of section III B 3, we have excluded these expenses from the carrier's T-88.

8. Pursuant to section III E of the Class Rate Order, the carrier's T-88 investment has been adjusted, where appropriate, to reflect the various adjustments detailed above. In addition, the following adjustments to the carrier's investment have been made:

(a) A downward adjustment has been made to reflect the actual profit-sharing liability for 1961, as determined for class rate purposes.

(b) In a prior subsidy case, certain extension and development costs were disallowed. In adjusting its T-88 investment for this disallowance, the carrier removed the unamortized portion of this item (\$96,000) from both debt and equity on a prorate basis. However, since the disallowed item was directly traceable to equity, it should have been removed from equity only, and we have adjusted the T-88 accordingly.

^{6/} A similar disallowance was made in North Central's 1961 profit-sharing determination. The carrier's argument that such of the assistant's time as was devoted to financing was concerned with debt financing and that the return element on debt does not include an allowance for such financing costs must be rejected. All appropriate costs of floating debt are includable in the return on debt investment, and the return on debt element embodied in the Class Rate adequately covers such costs. Further, any challenge to the return on debt element should have been made at the time the Class Rate was established, rather than indirectly in a profit-sharing proceeding. Our prior discussion of this matter is equally applicable in the current proceeding and is incorporated by reference herein. Order E-21319, pp. 4-5, September 23, 1964.

9. In accordance with section III F, which provides for recognition of actual taxes only, we have adjusted the carrier's computation of income taxes to take into account an investment tax credit of \$25,660.

North Central took the benefit of this credit in its tax return for 1962, but did not apply the credit for purposes of its T-88 tax computation, claiming that section 203(e) of the Revenue Act of 1964 requires the Board to ignore this tax saving for profit-sharing purposes. Acceptance of the carrier's T-88 would have the result of increasing the actual tax allowance to the extent of the tax credits.

The Board recently had occasion to review in detail the question whether the Revenue Act of 1964 required us to exclude investment tax credits from actual tax treatment for purposes of profit-sharing determinations for calendar year 1964 and subsequent years under Class Rate III.^{7/} Our review of the Revenue Act and its legislative history convinced us that the Congress intended only to prevent a flow-through of the credit to "consumers" in commercial rate cases and did not intend to preclude the application of the actual tax policy to investment tax credits in subsidy cases. Since the encouragement of development and expansion by other regulated industries and by unsubsidized airlines, which section 203(e) of the tax statute was intended to realize, is already provided for subsidized carriers by section 406(b) of the Federal Aviation Act, providing subsidy to cover taxes which the carriers do not pay would contravene the prohibition against providing subsidy in excess of the statutory "need." We would not read section 203(e) as incompatible with section 406 without a clear statement that the Congress desired such a result, and we have found nothing to indicate that Congress ever considered the consequences of section 203(e) in subsidy rate-making proceedings.

Moreover, the applicability to administrative determinations of excess profits and excess subsidy of a tax statute enacted to govern commercial rate cases appears even more remote. North Central did not raise objection to the Class Rate when it was established. While the tax statute was apparently intended to govern commercial rate cases in esse covering periods prior to enactment of the legislation,

we cannot conceive that when Congress in 1964 prohibited agencies, in the absence of taxpayer consent, from passing investment tax credit benefits through to consumers, it intended to change even commercial rates already fixed for earlier years, much less to make a retroactive change in a class subsidy rate established prospectively covering the year 1962. The Board's actual tax principle will continue^{8/} to govern our administrative determinations pursuant to class rates as well as other subsidy cases.^{9/} We will apply the credit to the tax allowance for North Central and make appropriate adjustments to investment.

^{7/} (Statement of Provisional Findings and Conclusions) Order E-21227, August 28, 1964, (Final Order) Order E-21311, September 22, 1964. Our discussion of the investment tax credit, set forth on pages 32-36 of Order E-21227, is hereby incorporated by reference herein.

^{8/} Bonanza Air Lines, Inc., 1962 Subsidy Refund, Order E-21137, July 30, 1964.

^{9/} Alaska Coastal-Ellis Airlines, Mail Rates, Orders E-20790, May 5, 1964, and E-20835, May 19, 1964; Aloha Airlines, Subsidy Mail Rates, Orders E-21138, July 30, 1964, and E-21179, August 11, 1964.

10. The carrier's Form T-88 showed that the subsidy payable under the formula, prior to reduction for profit-sharing, was greater than the amount it had reported on its Form 41. However, the related income tax liability was not adjusted upward to reflect the greater amount of subsidy payable under the formula. Accordingly, an appropriate adjustment has been made to income taxes. Correspondingly, the reported investment shown by North Central on its T-88 has been adjusted upward to reflect the net greater amount of subsidy after taking into account the related income tax liability.

With the revisions indicated above, and after reflecting the impact of such revisions in the related calculations under the formula, the amount of subsidy refund due from North Central for the calendar year 1962 has been determined to be \$556,103.

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Accordingly, IT IS ORDERED, That North Central Airlines, Inc., shall refund \$556,103 to the Government pursuant to the provisions of Class Rate I, for the calendar year 1962.

By the Civil Aeronautics Board:

HAROLD R. SANDERSON
Secretary

(SEAL)

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Mr. Daniel F. May
Treasurer
North Central Airlines, Inc.
6201 34th Avenue, South
Minneapolis, Minnesota - 55450

Feb. 10, 1965

Dear Mr. May:

A check for \$520,642 has been mailed to the carrier for subsidy as follows:

January, 1965	\$656,824
1/1-12/31/64 profit sharing	<u>106,109</u> \$762,933
1962 profit sharing refund per E-21663	556,103
Less Amount withheld	<u>313,812</u>
Balance of refund	<u>-242,291</u>
	\$520,642

Details of the \$106,109 adjustment are shown in the enclosure. A copy of Form 545 for December is returned herewith. Please note mileage corrections.

Sincerely yours,

/s/ Jack R. Herman, Chief
Carrier Payments Section
Office of Administration

Enclosures:

CAB Form 545, December, 1964, January, 1965

"Need" computation

Mileage corrections

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[281]

CAB Form 545
(Rev. 9-64)

CIVIL AERONAUTICS BOARD

Vou. No. 58213
Rec'd FEB 5 1965

Air Carrier's Claim For Subsidy

(Under Local Service Class Subsidy Rate)

INSTRUCTIONS: Complete Part I (space within bold lines) and forward to Carrier Payments Section, B-29, Civil Aeronautics Board, Washington, D.C. 20428, in original and five copies.

I. CARRIER'S CLAIM PER E- 21311				3. Month for which subsidy is claimed				
1. Carrier NORTH CENTRAL AIRLINES, INC.				January . 1965				
2. Address 55450 6201 - 34 Ave. S., Minneapolis, Minn.								
				II. FOR CAB ADJUSTMENT				
Plane Type (4)	Departures		Revenue Plane Miles (7)	Std. Available Seat Miles (000) (8)	Departures		Revenue Plane Miles	Std. Avail. Seat Miles (000)
	Actual (5)	Weighted (6)			Actual	Weighted		
DC-3	5,893	5,893	458,977	11,015				
CV	7,656	9,187	709,890	28,396				
	13,549	15,080	1,168,867	39,411				
9. Station (less one) days	7/31 + 24 - 31				2,163			
10. Length of hop (7) ÷ (5)					86.27			
11. Length of hop adjustment factor					09.70 %		%	
12. Actual departures per station-day (5) ÷ (9)					6.26			
13. Weighted departures per station-day (6) ÷ (9)					6.97			
14. Adjusted weighted departures per station-day (13) x (11)					6.25			
15. Rate per available seat mile					1,666.66 c		c	
16. Computed subsidy (gross) (8) x (15)					\$ 656,824		\$	
17. Frequency adjustment factor 8.00 ÷ (12)					%		%	
18. Formula subsidy (16)x(17)					\$ 656,824		\$	
19. Subsidy reduction adjustment					\$		\$	
20. Ad hoc adjustment					\$		\$	
21. Net subsidy (18)-(19)-(20)	245/240.52				\$ 656,824		\$ 656,824	
I certify that the above bill is correct and just according to the attached supporting statement, that the supporting statements are consistent with operating records, and that full payment therefor has not been received.								
<i>Bernard Sweet</i> (Signature)				Vice President-Finance (23) (Title)	February 4, 1965 (24) (Date)			

III. CAB DETERMINATION OF PAYMENT

	1/1/64-12/31/64 Jan 1965	Total
1. Adjusted claim for subsidy	7 894 121	
2. "Need"	7 036 810	
3. Prior payment	6 930 701	
4. Balance paid (Date 2/5/65 Sch. No. 51802)	106 109 656 824	520642 *
	295/296/14	

* Includes recapture of #242 291 additional P/S for 1962. Order E 2166 dated 1/1/65

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CAB Form 545
(Rev. 9-64)

CIVIL AERONAUTICS BOARD

Vou. No. 51-181
Rec'd JAN 6 1965

Air Carrier's Claim For Subsidy

(Under Local Service Class Subsidy Rate)

INSTRUCTIONS: Complete Part I (space within bold lines) and forward to Carrier Payments Section, B-29, Civil Aeronautics Board, Washington, D.C. 20428, in original and five copies.

I. CARRIER'S CLAIM PER E- 21311				3. Month for which subsidy is claimed				
1. Carrier <u>NORTH CENTRAL AIRLINES, INC.</u>				<u>December</u> <u>1964</u>				
2. Address <u>55450</u> <u>6201 - 34 Ave. S., Minneapolis, Minn.</u>				II. FOR CAB ADJUSTMENT				
Plane Type (4)	Departures		Revenue Plane Miles (7)	Std. Available Seat Miles (000) (8)	Departures		Revenue Plane Miles	Std. Avail. Seat Miles (000)
	Actual (5)	Weighted (6)			Actual	Weighted		
DC-3	5,680	5,680	439,495	10,548	5680	5680	439,501	10548
CV 34	7,675	9,210	709,782	28,391	7675	9210	709,770	28391
	13,355	14,890	1,149,277	38,939	13,355	14,890	1,149,271	38,939
9. Station (less one) days					2170		2170	
10. Length of hop (7) ÷ (5)					86.06		86.06	
11. Length of hop adjustment factor					89.54 %		89.24 %	
12. Actual departures per station-day (5) ÷ (9)					6.15		6.15	
13. Weighted departures per station-day (6) ÷ (9)					6.86		6.86	
14. Adjusted weighted departures per station-day (13) x (11)					6.14		6.14	
15. Rate per available seat mile					1.6862 \$		1.6862 \$	
16. Computed subsidy (gross) (8) x (15)					\$ 656,589		\$ 656,589	
17. Frequency adjustment factor 8.00 ÷ (12)					%		%	
18. Formula subsidy (16)x(17)					\$		\$	
19. Subsidy reduction adjustment					\$		\$	
20. Ad hoc adjustment					\$		\$	
21. Net subsidy (18)-(19)-(20)					\$ 656,589		\$ 656,589	

I certify that the above bill is correct and just according to the attached supporting statement, that the supporting statements are consistent with operating records, and that full payment therefor has not been received. 275/296.72Bernard Sweet (Signature)
Bernard Sweet (22) (Signature)Vice President-Finance
(23) (Title)January 5, 1965
(24) (Date)**III. CAB DETERMINATION OF PAYMENT**

1. Adjusted claim for subsidy
2. "Need"
3. Prior payment
4. Balance paid (Date 2/1/65 Sch. No. 51-181)

245/296.72

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Mileages

North Central

December, 1964

<u>From</u>	<u>To</u>	<u>Mileages</u>	<u>Departures</u>	
		<u>Claimed</u>	<u>CAB</u>	
			<u>Claimed</u>	<u>CAB</u>
CMX	GRR	325	329	
CLE	CLE	222	214	
CLE	GRB	381	382	
STE	EAU	100	98	
DLH	BRD	101	98	
ABR	BFF	362	358	
DVL	ATY	233	236	
VTP	ORD	226	224	

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CAB - Carrier Payments Section

"Need" Computation

Period: 1/1/64-12/31/64

NORTH CENTRAL

<u>A. Return element</u>	<u>Long-Term</u>	<u>Convertible</u>	<u>Common</u>	<u>Preferred</u>	<u>Total</u>
	<u>Debt</u>	<u>Debentures</u>	<u>Equity</u>	<u>Equity</u>	
3/31/64 Form 41	5571164	851500	3259028		9681692
6/30/64 Form 41	5466389	851500	3585527		9903416
9/30/64 Form 41	4936272	851500	3740682		9528457
10/31/64 Interim Report	4759801	851500	3806271		9417572
11/30/64 Interim Report	4643505	851500	3856293		9351298
12/31/64 Interim Report	5613050	851500	3854352		10318902
Average	\$ 5165030	\$ 851500	\$ 3683692		\$ 9700222
Annual rate	5.625 %	6.00 %	18.675 %	7.50 %	XXX
Return	\$ 290533	\$ 51090	\$ 687929		\$ 1029552
Percent of investment					10.61 %
1.50% band					1.50 %
Rate of return					12.11 %
Return element					\$ 1174677
Maximum rate 12.50%					
 <u>B. Breakeven need</u>					
Nonsubsidiy revenue					\$ 22428395
Operating expenses					\$ 27646408
Operating breakeven need					\$ 5218013
 <u>C. Income Taxes</u>					\$ 644100
Net Need					\$ 1156810

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[285]

NORTH CENTRAL AIRLINES, INC.
General Offices: 6201 Thirty-Fourth Avenue So. — Minneapolis, Minn.

February 25, 1965

Mr. Jack R. Herman, Chief
Carrier Payments Section
Office of Administration
Civil Aeronautics Board
Washington, D.C.

Dear Mr. Herman:

We have your letter of February 10, 1965, advising that a check for \$520,642 has been mailed to North Central for subsidy covering the period January, 1965, and profit sharing for 1964. In addition, your letter notes that an amount of \$242,291 is deducted as the balance of North Central's 1962 profit sharing refund.

You will recall that North Central objected to the Board's determination that \$556,103 was due as constituting the profit sharing refund for 1962. In particular, North Central is of the belief that the Board, pursuant to the Internal Revenue Code, was not authorized to consider the federal investment tax credit in determining a subsidy refund. We wish to advise you, therefore, that our acceptance of your check should in no way be construed as acquiescence by North Central to Order E-21163 and to the offset of \$242,291 and we do not waive any right to take further legal action in furtherance of our position.

Very truly yours,

NORTH CENTRAL AIRLINES, INC.

/s/ Daniel F. May
Treasurer

DFM:njp

CLASS RATE PROFIT SHARING SCHEDULES

GENERAL INSTRUCTIONS

The Local Service Class Subsidy Rate Order E-16485, adopted March 7, 1961, contains profit-sharing provisions, subjecting the annual subsidy otherwise due and payable to reduction to the extent that a carrier's earnings for calendar year 1961 exceed the fair and reasonable rate of return. In applying the provisions of the profit-sharing section of the Order, revenues, other income items, expenses, and investment are to be determined in accordance with the provisions of Section III of the Order.

The attached profit sharing schedules are prescribed as the standard format to be used by local service carriers claiming subsidy under the class rate. These schedules are required to be submitted by April 15, 1962 by all such carriers. The use of these schedules will enable the carriers to determine the amount of adjusted earnings under the class rate for the calendar year 1961, and will facilitate the Board's audit of final subsidy earnings under the class rate in Order E-16485 as amended.

Five sets of blank schedules are supplied, to be filled out in triplicate and forwarded to the Carrier Payments Section, Office of Administration, Civil Aeronautics Board, Washington 25, D. C. Two copies are to be retained by the carrier. In addition, an illustrative set of schedules is furnished to supplement the instructions for completing the forms.

For the most part the schedules are self-explanatory, many of them capable of being filled out on the basis of data taken from others in the group. Column headings and left-hand descriptions indicate the source of various data, and required computations are indicated when applicable.

The format includes hypothetical data for the purpose of better illustrating its use. Footnotes accompanying certain schedules also are intended to aid in illustrating the use thereof. It is understood that carriers will utilize footnotes or supplementary schedules to insure complete coverage.

A certification in the form attached of the report of earnings subject to profit-sharing shall be signed by an elective corporate officer, executive or director, or such other person as may be authorized by the carrier to sign the certification provided a written authorization disclosing the individual's name and title is filed with the Civil Aeronautics Board.

Specific instructions with regard to certain schedules follow below.

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INSTRUCTIONS FOR COMPLETION OF SCHEDULE A PROFIT SHARING COMPUTATION

Schedule A is used to show the computation of the amount of profit-sharing to be refunded to the Government. For carriers not in the profit-sharing bracket, this schedule should show the computation of the earnings deficiency. (Lines 1 through 18)

Since the profit-sharing adjustment itself causes a change in the recognized investment, the successive-step technique shown in this illustrative schedule should be followed by the carriers. The computations should be carried out until the difference in the return element "D" is less than \$100. The figure on line 31 in the last column represents the amount of profit sharing.

For illustrative purposes only, the tax effect of the refund is reflected at a 52% rate. In practice, however, the tax effect should reflect the actual composite Federal and state(s) tax rate.

It should be noted that the adjustment to common equity on line 6 is to be based upon the amount on line 29 only in the event the balance sheet reflects proper tax accruals equal to or in excess of the tax adjustment; otherwise the adjustment should be based upon the amount on line 31.

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INSTRUCTIONS FOR COMPLETION OF SCHEDULE R, S, T, U. INCOME TAX ADJUSTMENT

These schedules show the summary and detailed adjustments to federal and state income taxes related to adjustments for capital gains, nontransport ventures, and awards of retroactive subsidy. The basis for such adjustments is that if income from these three sources is not included in computing profit for purposes of profit-sharing, the related tax likewise should not be reflected.

Special instructions for filling out the required information are contained in footnotes on illustrative schedules R, S, and T.

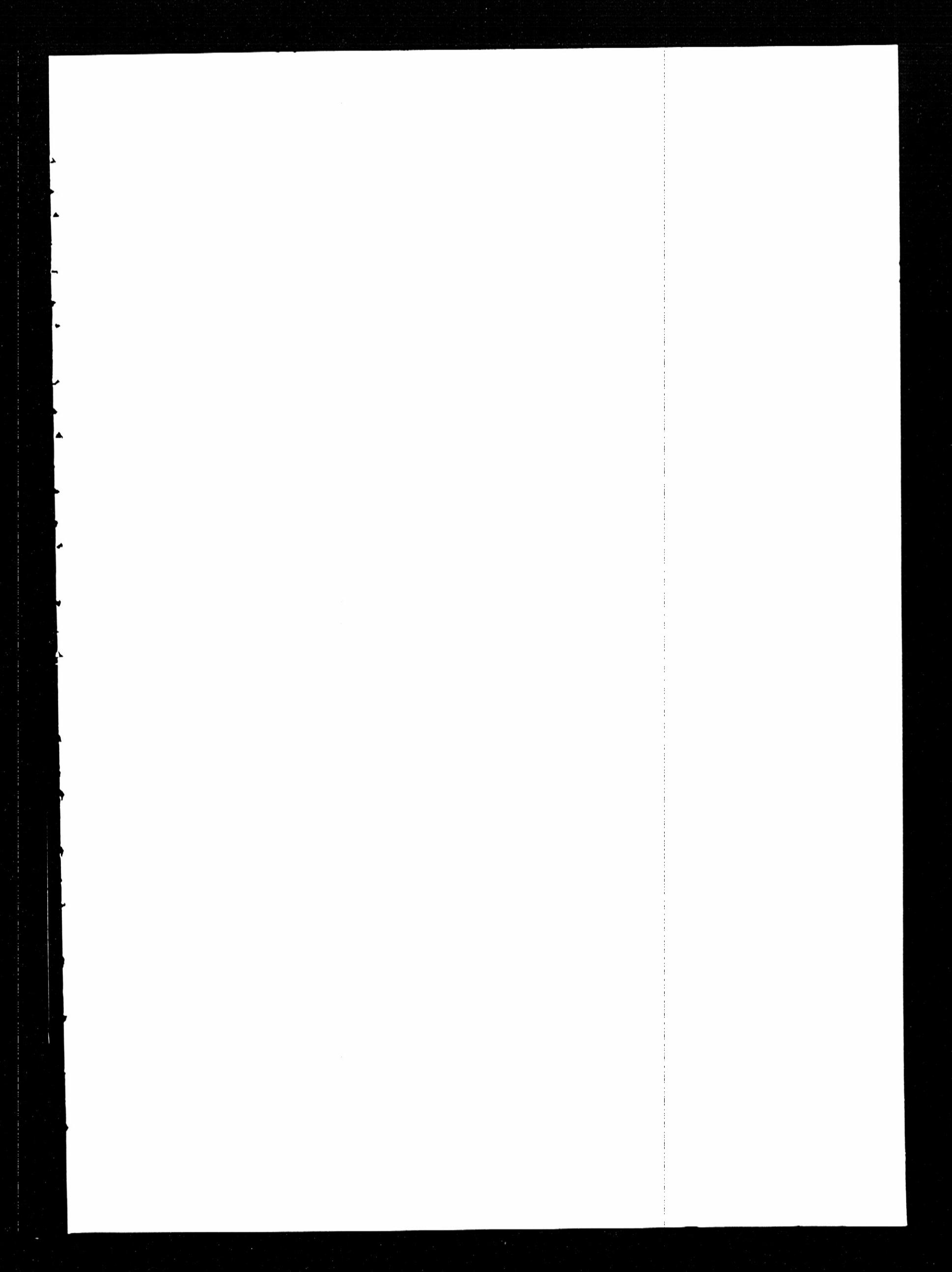
Copies of all applicable Federal and State(s) tax returns are to be submitted.

Carriers whose tax year is on other than a calendar year basis are required under the Order to submit a pro-forma tax return for 1961. A reconciliation of such pro forma return with the carrier's reported operating results should be submitted.

Schedule T is to be filled out by the carrier if net capital gains were realized during the period April 6, 1956 through December 31, 1961. Because of the 5-year loss carry-forward provisions, since the year 1956 can be affected by results in 1951, tax return data are required for the years 1951 through 1961 if there were capital gains in 1956. However, the necessity for filling in data for years before 1956 is governed by the earliest year from April 6, 1956 in which capital gains were realized. The tabulation below shows the data required by

years, due to the realization of capital gains:

<u>Capital Gains During:</u>	<u>Schedule T Data Required from:</u>
1956	1951
1957	1952
1958	1953
1959	1954
1960	1955
1961	1956



BRIEF FOR RESPONDENT

IN THE
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 19,209

NORTH CENTRAL AIRLINES, INC.,

Petitioner,

v.

CIVIL AERONAUTICS BOARD,

Respondent.

ON PETITION FOR REVIEW OF AN ORDER
OF THE CIVIL AERONAUTICS BOARD

United States Court of Appeals
for the District of Columbia Circuit

FILED SEP 22 1965

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Civil Aeronautics Board.

(i)

COUNTERSTATEMENT OF QUESTIONS PRESENTED

In respondent's view, the questions for decision are:

1. Whether the Board's determination of petitioner's subsidy refund for 1962 constitutes an order reviewable under section 1006 of the Federal Aviation Act?
2. Whether the Board's treatment of petitioner's investment tax credit in determining its profit-sharing refund for 1962 was required by (a) the applicable outstanding final subsidy rate order, and (b) the "need" limitation of section 406(b)(3) of the Act?
3. Whether section 203(e) of the Revenue Act of 1964 should be construed as (a) amending section 406 of the Federal Aviation Act, and (b) retroactively amending the subsidy rate order governing petitioner's 1962 operations?

(iii)

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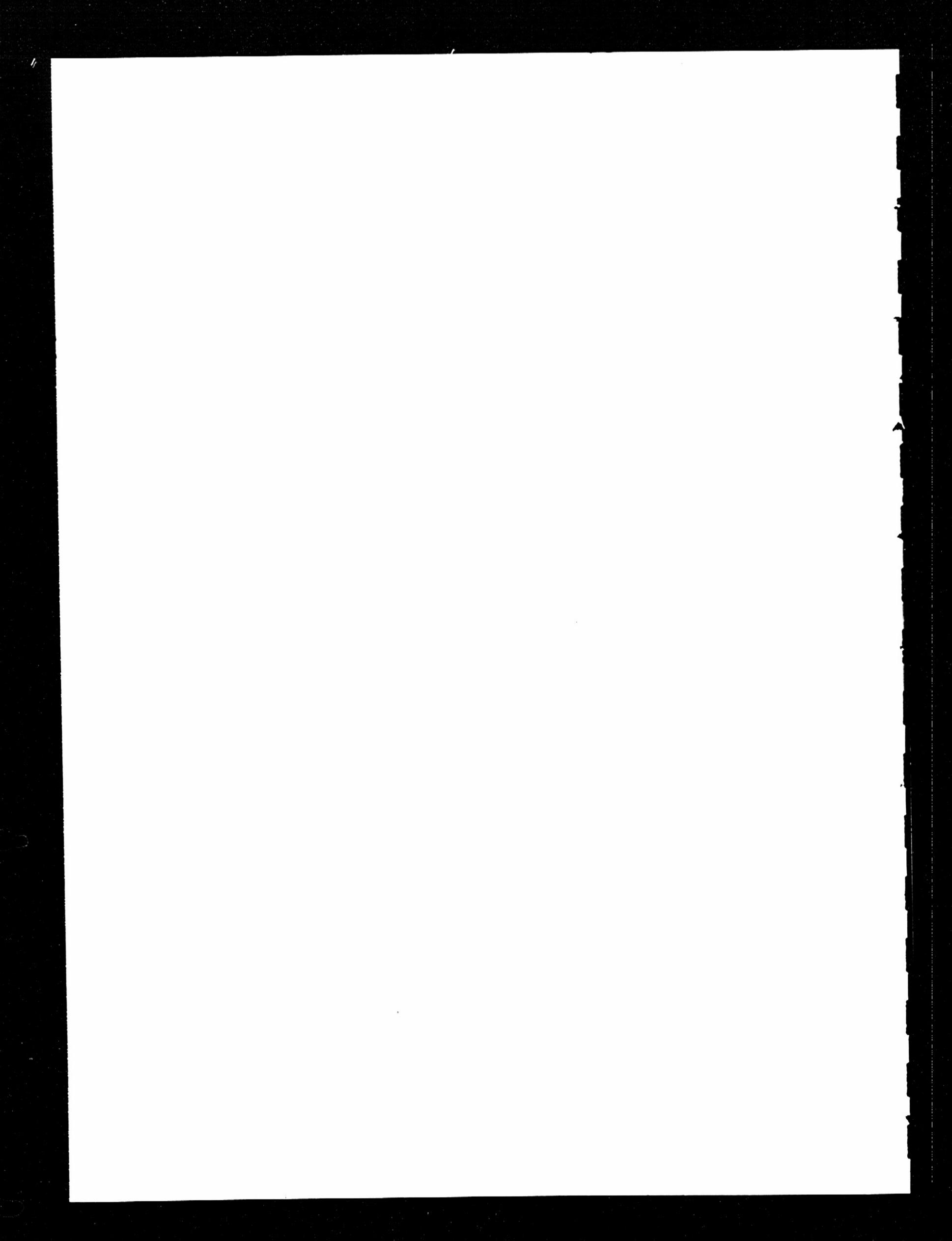
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IN THE
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 19,209

NORTH CENTRAL AIRLINES, INC.,

Petitioner,

v.

CIVIL AERONAUTICS BOARD,

Respondent.

ON PETITION FOR REVIEW OF AN ORDER
OF THE CIVIL AERONAUTICS BOARD

BRIEF FOR RESPONDENT

COUNTERSTATEMENT OF THE CASE

Petitioner seeks review of the Board's treatment of one \$25,660 item in its computation of a "profit-sharing" refund of \$556,103 due from petitioner for the year 1962. The computation was made in Order E-21663 (January 11, 1965; Tr. 273), pursuant to the profit-sharing provisions of Local Service Class Subsidy Rate Investigation (Class Rate I), 34 C.A.B. 416, 418, 428 (1961)(Tr. 6, 77), the final rate order fixing 1961-62 subsidy rates for petitioner and the other local-service airlines. On February 10, 1965, thirty days later, the Board recouped the balance of the refund thus found due by offsetting it against petitioner's regular subsidy payment for January 1965

^{1/}
(Tr. 280). The petition for review was filed March 9, 1965.

The sole item still in dispute is the Board's treatment of the so-called "investment tax credit" claimed by petitioner on its 1962 federal income tax returns. The Board ruled that under the outstanding rate order this credit must be taken into account in determining petitioner's after-tax earnings, whereas petitioner argued that the credit should be ignored. The result of the Board's ruling was to increase petitioner's after-tax profit subject to sharing by \$25,660, and consequently to increase the government's share thereof by some \$20,740.
^{2/}

The Class Subsidy Rate I Order

Under section 406 of the Federal Aviation Act (infra, p. 52), air carriers holding certificates authorizing them to transport mail receive two forms of mail pay. All such carriers receive "service" mail pay, which is designed to compensate them fairly for the actual transportation of mail, and for the equipment and facilities they maintain which are used and useful for such transportation. In

^{1/} This is the Board's customary method of recovering subsidy overpayments, including profit-sharing refunds. Somewhat more than half of the refund as finally determined had previously been withheld by the Board on an estimated basis, so that only \$242,291 still remained due. Petitioner took no affirmative steps to remit this balance prior to the Board's offset action.

^{2/} At several points in its brief (Pet. Br. 5, 6, 7, 12, 27, 44) petitioner incorrectly states or implies that the Board reduced its subsidy by the full amount of its investment credit. The actual computation is discussed in more detail hereafter (infra, pp. 4, 9).

^{3/} Until 1953, both service and subsidy mail pay were disbursed by the Post Office, although the Board had been distinguishing between the two kinds of rates for a long time prior thereto. Under Reorganization Plan No. 10 of 1953, 67 Stat. 644, 5 U.S.C. 133z, the function of paying subsidy was shifted to the Board, while the Post Office continued to disburse service mail pay. This division of functions was later codified in section 406(c) of the Federal Aviation Act of 1958 (infra, p. 52).

addition, a number of carriers (including petitioner) receive "subsidy" mail pay. Under section 406(b)(3) of the Act, this pay is based, not on the cost of carrying the mail, but on the "need" of the carrier for funds to make up its operating losses and to give it, after taxes, a fair return on its investment. Those carriers who are able to meet their operating expenses and earn a fair return out of their commercial revenues do not receive subsidy.^{4/}

Until 1961, with one exception, the Board had always determined subsidy rates on a carrier-by-carrier basis, constructing an individual rate formula for each carrier based on its own experienced or anticipated revenues and costs. In the Local Service Class Subsidy Rate Investigation, 34 C.A.B. 416, 418, 428 (1961), the Board determined that the thirteen local-service carriers constituted a sufficiently homogenous group so that their "need" for subsidy under section 406(b)(3) could be met by a single class rate applicable to all of them. The Board recognized, however, that under this rate ("Class Rate I"), some carriers could be expected to receive more than a fair rate of return on investment (34 C.A.B. at 440). Consequently, after fixing a "formula" subsidy rate of so much per available seat-mile flown, based on certain operational factors, the Board provided for a system of profit-sharing as an integral part of the subsidy rate

^{4/} The Board's formal finding in the rate order here at issue, for example, was "that the fair and reasonable rates of compensation on and after January 1, 1961, to be paid" each local-service carrier "for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith . . . are the sum of (a) the service mail rate as heretofore and hereafter established for the carrier by Board orders pursuant to section 406(c) of the Act and (b) the subsidy rate for the carrier as set forth in" the class rate order (34 C.A.B. at 419, 443-4). The order's subsidy formula included no factor relating to the actual transportation of mail by the carriers.

order. It provided that each carrier's profit after taxes should be ascertained following the close of each calendar year, and described in detail how this profit should be calculated. If the carrier's after-tax profit were less than its "fair and reasonable differentiated rate of return" on its recognized investment (detailed rules also being given for the computation of this rate of return and investment) ^{5/} no profit-sharing would take place. If the carrier's profit should exceed this rate of return, the carrier would be required to refund out of its "formula" subsidy an amount equal to 50 percent of such excess; if its return should exceed 15 percent, subsidy ^{6/} would be reduced by 75 percent of this latter excess.

The Class Rate I order made the following provision with respect to the recognition of income taxes in computing after-tax profits subject to profit-sharing (34 C.A.B. at 426):

5/ The carrier's "fair and reasonable differentiated rate of return" was defined as comprising a return of 5.50 percent on its debt capital, 7.50 percent on its preferred stock, and 21.35 percent on its common equity capital, subject to a lower limit of 9 percent and an upper limit of 12.75 percent on overall investment. These component return elements (other than that for preferred stock) were carried over from the Board's previous decision in Rate of Return, Local-Service Carriers, 31 C.A.B. 685 (1960). The 21.35 percent return figure for equity capital was there derived by taking the observed cost of equity capital to the "Medium Eight" trunkline carriers (i.e., all those but the "Big Four"), and adding a bonus of 50 percent, plus 15 percent for flotation costs (31 C.A.B. at 686-8).

6/ In the actual computation, it is necessary to take account of the fact that profit-sharing itself reduces earnings, hence year-end investment, hence the base return not subject to profit-sharing. Consequently, several successive tentative refund calculations must be made, and the government's share as ultimately determined is always somewhat greater than that shown by the first tentative calculation. (See Tr. 99, 179, 267, 289-90, lines 6 and 29). Finally, pursuant to section III G of the class rate order, 34 C.A.B. at 426, the subsidy refund thus calculated is increased to compensate for the tax refunds the carrier will subsequently be able to claim as a result of the subsidy refund.

"F. Income Taxes. -- Federal and State income taxes shall be determined on the basis of the carrier's income tax returns for each year as submitted to the taxing authorities, with such amendments or revisions (including tax carryback and carry-forward credits) as may have been filed as of the date of the final determination of excess profits (or an earnings deficiency) under this order; . . ."

Class Rate I was made final on March 7, 1961, as to all but four of the local-service carriers, including petitioner (34 C.A.B. ^{7/} at 418). No carrier sought judicial review of this order, which remained in effect through the end of 1962, being replaced as of ^{8/} January 1, 1963, by a new rate known as "Class Rate II".

The Investment Tax Credit

On October 16, 1962, the Internal Revenue Code was amended so as to provide for a credit against income taxes otherwise payable of a specified percentage of the taxpayer's "qualified investment" for the year -- i.e., the amount invested by the taxpayer in certain types of productive facilities or equipment. P.L. 87-834, Oct. 16, 1962, 76 Stat. 962, 26 U.S.C. 38, 46-48. Controversy subsequently arose as to how this credit should be treated by regulatory agencies in commercial rate cases. Several agencies (particularly the Federal Power and Communications Commissions) held that the benefit of the investment tax credit should "flow through" to the customers of the utilities regulated by them in the form of lower rates. To settle the controversy, Congress enacted section 203(e) of the Revenue Act

^{7/} Later in 1961 the remaining four withdrew their objections and the rate was likewise made final as to them.

^{8/} Local Service Class Subsidy Rate Investigation (Class Rate II), Order E-19340 (March 1, 1963), which followed an order reopening the rate as to all thirteen local service carriers as of January 1, 1963 (Order E-19118, December 20, 1962).

of 1964, (infra, p. 56-7), which provided in pertinent part as follows:

"It was the intent of the Congress in providing an investment credit under section 38 of the Internal Revenue Code of 1954, . . . to provide an incentive for modernization and growth of private industry (including that portion thereof which is regulated). Accordingly, Congress does not intend that any agency or instrumentality of the United States having jurisdiction with respect to a taxpayer shall, without the consent of the taxpayer, use . . . (2) in the case of any other property ^{9/}, any credit against tax allowed by section 38 of such Code, to reduce such taxpayer's federal income taxes for the purpose of establishing the cost of service of the taxpayer or to accomplish a similar result by any other method."

Petitioner made "qualified investments" during 1962, claimed the investment credit on its 1962 federal income tax returns, and as a result secured a tax reduction of \$25,659.68 (Tr. 155, 159). After closing its books for 1962, petitioner filed with the Board the required Form T-88, "Class Rate Profit-Sharing Schedule", showing a total profit-sharing refund for 1962 of \$309,011 (Tr. 99). In its profit computation, petitioner treated its 1962 investment tax credit as non-existent. The Board's staff subsequently audited petitioner's profit-sharing report and proposed a number of adjustments, among them one relating to petitioner's 1962 investment tax credit, which the staff proposed to recognize for profit-sharing purposes as a reduction in taxes paid (Tr. 177, 187). Petitioner disagreed with this and other adjustments proposed by the staff, and an exchange of correspondence ensued, during the course of which petitioner submitted a letter and memorandum contending that the proposed treatment of its investment tax credit was contrary to the Congressional intent (Tr. 238, 242). No formal hearing was held,

^{9/} Separate provisions, not here material, governed the treatment of the credit with respect to "public utility property" as defined in the Code.

however, the Board taking the view that none was required by law
10/
or called for by the circumstances.

The Board's Refund Determination

In the order here sought to be reviewed (Tr. 273), the Board fixed petitioner's 1962 profit-sharing subsidy refund at the \$556,103 figure. At the outset, the Board stressed that it was not determining petitioner's "need" for subsidy or making any other rate-making determination under section 406 of the Act (Tr. 274):

"This form [Form T-88] and the provisions of the class rate which it effectuates are so designed that the administration of profit-sharing and subsidy refund does not involve rate-making determinations, but solely the ascertainment of the pertinent facts and the application of the provisions of the formula to those facts. 4/"

" 4/ Since Class Rate I is final, as is true of all final rates, its provisions are not open to contest retroactively and are not in issue in determinations such as the instant one."

The order then went on to detail the adjustments which account for the difference between the \$556,103 figure and the one originally submitted by petitioner (Tr. 274-6). Of these adjustments, only the one relating to the investment tax credit is here challenged. As to this issue, the Board adopted the position of its staff. The Class Rate I order, the Board held, provided for recognition of actual taxes only in the profit-sharing computation, whereas petitioner's Form T-88, by ignoring the \$25,660 tax reduction resulting from its investment tax credit, sought recognition for more taxes than it had actually paid or would pay (Tr. 277).

10/ See North Central Airlines, Subsidy Refund-1961, Order E-21319 (Sept. 23, 1964), p. 2.

11/ All of the Board's orders determining profit-sharing subsidy refunds have included this or substantially identical language.

The Board noted that it had recently had occasion to review in detail the question whether section 203(e) of the Revenue Act of 1964 required exclusion of a carrier's investment tax credit in profit-sharing computations.^{12/} As to the intent of Congress in enacting section 203(e), the Board observed (Tr. 277):

"Our review of the Revenue Act and its legislative history convinced us that the Congress intended only to prevent a flow through of the credit to "consumers" in commercial rate cases and did not intend to preclude the application of the actual tax policy to investment tax credits in subsidy cases. Since the encouragement of development and expansion by other regulated industries and by unsubsidized airlines, which section 203(e) of the tax statute was intended to realize, is already provided for subsidized carriers by section 406(b) of the Federal Aviation Act, providing subsidy to cover taxes which the carriers do not pay would contravene the prohibition against providing subsidy in excess of the statutory "need". We would not read section 203(e) as incompatible with section 406 without a clear statement that the Congress desired such a result, and we have found nothing to indicate that Congress ever considered the consequences of section 203(e) in subsidy ratemaking proceedings."

Moreover, the Board observed that to apply section 203(e) to petitioner's 1962 profit-sharing computation would amount to retroactive amendment of an outstanding final rate order:

"While the tax statute was apparently intended to govern commercial rate cases in esse covering periods prior to the enactment of the legislation, we cannot conceive that when Congress in 1964 prohibited agencies, in the absence of taxpayer consent, from passing investment tax credit benefits through to consumers it intended to change even commercial rates already fixed for earlier years, much less to make a retroactive change in a class subsidy rate established prospectively covering the year 1962."

12/ Local Service Class Subsidy Rate Investigation (Class Rate III), Order E-21227 (Aug. 28, 1964), pp. 32-36. The Board incorporated this discussion by reference in Order E-21663, and we have reprinted it as an appendix to this brief (infra, p. 61-4).

Accordingly, in its final calculation (Tr. 267-9), the Board reduced petitioner's recognized federal income tax by the amount of the \$25,660 investment tax credit, thereby increasing petitioner's after-tax profit subject to profit-sharing by a like amount and increasing the Government's share of that profit by approximately ^{13/} \$20,470. As previously noted, the Board deducted the balance of the refund as thus determined from petitioner's next monthly subsidy payment. Petitioner notified the Board that its acceptance of this subsidy check should not be construed as acquiescence in the Board's 1962 profit-sharing determination, particularly as regards the investment tax credit issue (Tr. 285); shortly thereafter, it filed its present petition for review.

STATUTES INVOLVED

The pertinent provisions of the Federal Aviation Act of 1958, the Revenue Act of 1964, the Administrative Procedure Act, the Transportation Act of 1940, and the Judicial Code are set forth in Appendix A hereto (infra, pp. 51-59).

13/ Since petitioner in 1962 earned more than 15 percent on its investment and hence fell in the 75 percent profit-sharing bracket under the Class Rate I order, 34 C.A.B. at 421-2, the increase of \$25,660 in its after-tax profit resulting from recognition of its investment tax credit had the effect of increasing the government's share of that profit, in the first tentative calculation, by 75 percent of that amount, or \$19,245. For reasons previously explained (supra, p. 4n.), relating to the way in which profit-sharing is recursively computed, the ultimate figure for the government's share is the slightly larger one given in the text. The point is that under the workings of the profit-sharing system, the increase in the government's share of profits resulting from the recognition of the investment tax credit is always less than the amount of that credit. Consequently, every subsidized carrier retains at least part of the benefit of the credit; carriers earning too little to be subject to profit-sharing, of course, retain the full benefit.

SUMMARY OF ARGUMENT

I

The Court should dismiss the petition herein for lack of jurisdiction on the same grounds as in Mohawk Airlines v. Civil Aeronautics Board, 117 U.S. App. D.C. 326, 329 F.2d 894 (1964). As there, the Board's action here constituted not an order reviewable under section 1006 of the Federal Aviation Act, but a statement of intention to recover an overpayment of subsidy by offset pursuant either to section 322 of the Transportation Act or to the government's common-law right of offset. The mere difference in form between the Board's actions in Mohawk and here is not controlling. Petitioner's argument, that the present order bound it to tender the refund to the Board and subjected it to penalties for failure to do so, begs the question and ignores the Board's consistent practice and interpretation of the nature of its actions in these cases. Petitioner's contention, that the 1958 amendment to section 322 of the Transportation Act made it inapplicable to the recovery of subsidy overpayments, is irrelevant because in that event the Board would be acting under its common-law right of offset, and still not under the Federal Aviation Act. In any case, the legislative history of the 1958 amendment shows no such change as petitioner suggests was intended.

II

The Board's treatment of petitioner's investment tax credit for 1962 profit-sharing purposes was required by the Board's "actual tax" policy, which calls for recognition only of taxes actually paid or

payable in subsidy determinations. That policy has been consistently followed by the Board since 1951, and has been previously applied to other "incentive" tax changes. Despite petitioner's efforts to twist the language of the Class Rate I order, therefore, it is plain that this order embodied the "actual tax" policy, which the Board was accordingly required to follow in computing petitioner's 1962 refund. As the cases make clear, furthermore, the "actual tax" policy is simply an expression of the statutory "need" and "all other revenue" limitations on subsidy payable under section 406(b)(3) of the Act, so that the Board had no discretion to depart from that policy unless it is concluded that Congress has amended section 406.

III

Section 203(e) of the 1964 Revenue Act, which does not expressly amend section 406, should not be held to do so impliedly. First, amendments by implication are not favored. Second, the language of section 203(e), plainly directed to ordinary utility and carrier commercial rate cases, does not necessarily apply to subsidy determinations. The purpose of subsidy, which is promotional, is very different from that of commercial rate regulation; the Board has frequently applied different principles in these two classes of cases; and court decisions make clear that when the special requirements and limitations of section 406(b)(3) conflict with ordinary rate-making principles, the former prevail. "Need", the central fact to be determined in subsidy cases, is moreover not equivalent to "cost of service", a term

of art connoting commercial rate regulation. Third, the legislative history of section 203(e) shows no Congressional intent to affect subsidy determinations by the Board under section 406, but on the contrary shows an exclusive concern to prevent regulatory agencies from "flowing through" the benefit of the investment tax credit to the customers of the utilities they regulate. The principal references to the Board in the legislative debates refute any notion that section 203(e)'s sponsors intended its application to subsidy cases. Finally, the purposes of section 203(e) will not be frustrated by the Board's refusal to grant subsidy in the amount of the investment tax credit, since carriers of petitioner's class already have been subsidized to the extent necessary to promote modernization by private investment in new and more efficient equipment.

IV

Even if section 203(e) could be construed as amending section 406, such an amendment would not apply retroactively to change the terms of Class Rate I, an outstanding final rate order. The principle of rate finality is deeply embedded, and Congress has carefully respected it in the past; there is no indication whatever it intended to breach that principle here. Petitioner's argument that no breach of finality would be involved in the result it seeks is merely an ingenious quibble. Petitioner could, by reopening the rate during 1962, have avoided the issues of rate finality and retroactive amendment, but chose instead to go on accepting the extremely generous benefits of Class Rate I; it should not now be heard to seek a retroactive change in a single provision of that order.

ARGUMENT

I. The Court lacks jurisdiction because the action of the Board here at issue does not constitute an order reviewable under section 1006 of the Federal Aviation Act.

We submit that this Court should dismiss the petition for review herein on exactly the same grounds that it recently dismissed a similar petition in Mohawk Airlines v. Civil Aeronautics Board, 117 U.S. App. D.C. ^{114/} 326, 329 F.2d 894 (1964). In that case the Board notified the carrier by letter that it had determined an overpayment of subsidy for a prior period, and would deduct the amount thereof from the carrier's next monthly payment of current subsidy. The Board's determination was based on its audit of the carrier's records and its interpretation of the carrier's prior subsidy rate order. In dismissing the carrier's statutory review petition for lack of jurisdiction, this Court said (329 F.2d at 896-7):

"It seems clear that the Board performs two separate and distinct functions with respect to payment for the air transportation of United States mail: (a) as authorized by the Federal Aviation Act, it fixes mail rates by orders, entered after notice and hearing, which are reviewable under section 1006; (b) as authorized by the Transportation Act [49 U.S.C. 66], it first pays carrier's claims as presented, then audits them and deducts any overpayments disclosed by the audits from amounts subsequently found to be due to the carriers involved. The second function is not performed by orders subject to review, but by interpretation of the mail pay orders theretofore entered. We think the letter of May 15, 1963

114/ The Court held that the petitioner there had a fully adequate remedy in the Court of Claims under 28 U.S.C. 1491. That court has also been held the proper forum for adjudication of disputes regarding the payment or withholding of maritime subsidies, see American President Lines v. Federal Maritime Board, 98 U.S. App. D.C. 259, 235 F.2d 18 (1956); American President Lines v. United States, 291 F.2d 931 (Ct. Cl. 1961); and of mail pay due other types of carriers, see United States v. New York Central R. Co., 279 U.S. 73, 77 (1929); United Fruit Co. v. United States, 168 F. Supp. 549 (Ct. Cl. 1958).

was not an order of the Board in any sense; certainly it was not an order issued by the Board under the Federal Aviation Act, but rather was a statement of intention to act under section 322 of the Transportation Act. So, even if the letter could be regarded as an order under the latter Act, it was not reviewable under section 1006 of the Federal Aviation Act." (emphasis added) 15/

The situation here is exactly comparable. Petitioner's subsidy for the year 1962 is completely governed by the Class Rate I order, which constituted a final rate-making determination by the Board under section 406 of the Act. That order was unquestionably reviewable under section 1006 when first adopted, but the time for such review has long since passed. As the Board took pains to stress (see supra, p. 7), Order E-21663 does not constitute a rate-making determination under section 406 of the Act. On the contrary, the class rate is so designed, including the profit-sharing provisions thereof, that all the Board is required to do is audit the carrier's reports, ascertain the facts, and apply the express terms of the class rate order to determine the subsidy refund due, if any. No issues of policy or discretion are involved; while it may become necessary for the Board to interpret the class rate order, it is bound to be guided by the original intent and meaning of that order, and may not retroactively amend the order under the guise of "interpretation". 16/

15/ The Court went on to hold that it similarly had no jurisdiction under section 10 of the Administrative Procedure Act, 5 U.S.C. 1009. Petitioner here does not appear to suggest that the Administrative Procedure Act would create jurisdiction to review if section 1006 did not. See Schwab v. Quesada, 284 F.2d 140 (C.A.3, 1960); City of Dallas v. Rentzal, 172 F.2d 122, 123 (C.A. 5, 1949).

16/ This is in accordance with the finality principle of Trans-continental & Western Air v. Civil Aeronautics Board, 336 U.S. 601 (1949), which forbids the Board to amend retroactively an outstanding final rate order which has not been duly reopened.

In seeking to distinguish Mohawk, petitioner makes much of the fact that the Board here embodied its determination in a formal "order", bearing a serial number and printed on green paper as are the Board's other orders. We submit that this mere difference in form -- which results from the fact that profit-sharing determinations under the class rate are considered to be of greater general interest than overpayment determinations following audits under individual-carrier rates, such as was involved in Mohawk -- should not be controlling.

The controlling fact, we submit, is that the Board has not treated its profit-sharing refund determinations under the class rate orders as having the conclusory, mandatory force of orders in which the Board exercises ^{17/} its quasi-legislative and/or quasi-adjudicatory powers under the Act. ^{18/} It has consistently refused to hold formal hearings on the

17/ On the one hand, even an informal letter may constitute a reviewable order under some circumstances; see Mid-Valley Distilling Corp. v. DeCarlo, 161 F.2d 485 (C.A. 3, 1947); United States v. Bass, 215 F.2d 9 (C.A. 8, 1954). On the other hand, there are many circumstances in which an agency statement issued with the full formalities of an "order" is held not to be judicially reviewable; see United States v. Los Angeles & S.L.R. Co., 273 U.S. 299, 309-10 (1927); American President Lines v. Federal Maritime Comm'n, 114 U.S. App. D.C. 418, 316 F.2d 419 (1963); California Oregon Power Co. v. Federal Power Comm'n, 99 U.S. App. D.C. 263, 239 F.2d 426 (1956); Helco Products Co. v. McNutt, 78 U.S. App. D.C. 71, 137 F.2d 681 (1943). As these latter-cited cases show, the fact that an agency statement interprets its governing statute or prior orders does not in itself make the statement judicially reviewable.

18/ Under section 1006(a), an order issued pursuant to the Act is ordinarily incontestable unless review is sought within 60 days; under section 1006(e), findings in such an order are conclusive if supported by substantial evidence; under section 901 (infra, p. 54), civil penalties of up to \$1,000 per day may be assessed for failure to comply with the command of such an order, while willful failure can draw various criminal penalties under section 902 (infra, p. 55). If the Court should hold the instant action to constitute an "order" under the Act, these consequences no doubt would attach, despite the Board's intent that they should not.

factual issues presented by such determinations, such as it would be required to hold if it were acting under section 406(a); it has taken the view that since its fact-findings are not conclusive, it can act in a purely administrative way, by informal conference and correspondence.^{19/} Nor have carriers in fact been called upon to tender to the Board the refunds thus determined, or threatened with the penalties provided in the Act for failure to do so; on the contrary, in profit-sharing cases as in Mohawk and innumerable prior individual-carrier subsidy refund cases, the Board has uniformly collected the refund due by offsetting it against current subsidy payments, pursuant to section 322 of the Transportation Act (infra, p. 58).^{20/} We submit that the Board's consistently followed interpretation of the nature of its own actions should be controlling -- particularly where, as we have seen, this interpretation deprived petitioner of no rights and affords it a fully adequate remedy.

^{19/} See, e.g., North Central Airlines, Subsidy Refund - 1961, Order E-21319 (Sept. 23, 1964), p. 2.

^{20/} Petitioner's assertion that Order E-21663 subjected it to civil and criminal penalties under sections 901 and 902 of the Act (infra, pp. 54-5) simply assumes the desired conclusion, that the Board's action constitutes an "order" under the Act. If, as the Court held in Mohawk, it is simply a statement of intention to act under the Transportation Act, then of course the penalty provisions of sections 901-2 would not apply.

If petitioner were correct in its assertions as to the possible penalties for failure to remit the refund determined in Order E-21663, its subsequent actions would be difficult to understand. Although it was contesting only the treatment of a single \$25,660 item, it made no move to pay the large remaining balance of the refund prior to the Board's offset action -- thus, on its own theory, subjecting itself to civil penalties of \$30,000 (30 days x \$1,000 a day) whether or not it ultimately prevailed on the investment tax credit issue.

Petitioner argues, however, that the 1958 amendment to section 322 of the Transportation Act has so narrowed the scope of that section that it no longer stands as authority for the Board to collect overpayments of subsidy by offset against the carrier's later subsidy bills; hence, petitioner contends, the Board's action can no longer be characterized as "a statement of intention to act under section 322",
^{21/} as in Mohawk (supra, pp. 13-14). Even if this were true, it would by no means follow, as petitioner would have it, that the Board's action can therefore only be characterized as an order under the Federal
^{22/} Aviation Act. The government's right to collect debts due it by offset existed prior to, and still exists independently of, the Trans-
^{23/} portation Act and for that matter the Federal Aviation Act. Thus, if the Board here did not act under section 322, it acted under the government's common-law right of offset; in neither event is its action a final "order" reviewable under section 1006.

Moreover, petitioner's analysis of the purpose and effect of the 1958 amendment to section 322 is erroneous. Prior to 1958, that section

^{21/} The 1958 amendment to section 322, 72 Stat. 860, was in terms inapplicable to the transactions involved in Mohawk.

^{22/} Petitioner so argues (Br. 45) on the basis that Order E-21663 "pertains to, and is in furtherance of, subsidy rates established pursuant to section 406 of [the Federal Aviation] Act." Precisely the same statement could be made about the "order" in Mohawk.

^{23/} United States v. New York, N.H. & H. R. Co., 236 F.2d 101, 105 (C.A. 1, 1956), rev'd on other grounds, 355 U.S. 253 (1957); accord, United States v. DeQueen & E.R. Co., 271 F.2d 597, 600 (C.A. 8, 1959). The considerations which motivated the original enactment of section 322 are discussed at length in United States v. New York, N.H. & H. R. Co., 355 U.S. 253 (1957), supra. The legislative history of the 1958 amendment (see infra, pp. 18-19) gives no indication whatever that Congress intended to abolish this common-law right of offset under circumstances such as those here presented.

provided that carriers' bills for the "transportation of United States mail and of persons or property for or on behalf of the United States" should be paid upon presentation, "but the right is reserved to the United States Government to deduct the amount of any overpayment to any such carrier from any amount subsequently found to be due such carrier." (emphasis added) The 1958 amendment changed the words "overpayment to" to "overcharges by" in the foregoing, and added the following definition of "overcharges":^{24/}

"The term 'overcharges' shall be deemed to mean charges for transportation services in excess of those applicable thereto under the tariffs lawfully on file with the Interstate Commerce Commission and the Civil Aeronautics Board and the charges in excess of those applicable thereto under rates, fares, and charges established pursuant to section 22 of this title."

Petitioner contends that, since subsidy rates are governed neither by tariffs nor by 49 U.S.C. 22, an overpayment of subsidy cannot be an "overcharge" under the new definition, so that section 322 is no longer authority for recovering such an overpayment by offset.^{25/}

This restrictive reading of the 1958 amendment, however, makes no sense in terms of the Congressional purpose. Section 322 as amended still purports to require the payment of carrier bills for transporting the mail on presentation, before audit, and it strains credulity to suppose that Congress would eliminate all provision for recovery of overpayments of such bills disclosed by subsequent audits. In fact, the legislative history shows that Congress's overriding concern in the 1958

24/ Certain limitations periods, not here relevant, were also added.

25/ This would apply equally, of course, to overpayments of "service" air mail pay and railroad mail pay, since neither are governed by tariffs or by 49 U.S.C. 22.

amendatory act was to put the government on a par with private shippers, principally by setting uniform limitations periods on actions for the collection or recovery of transportation charges. The stated purpose of limiting the offset procedure of section 322 to "overcharges" as above defined was to put an end to a government practice (unavailable to private shippers) of determining and offsetting "overpayments" of freight charges under section 322 where the charges were strictly in accord with the carrier's tariffs, but the Government believed the tariff rates themselves to be unlawful.^{26/} The legislative history is wholly devoid of any reference to the handling of mail-pay claims, or any indication that a change in this area was desired. To read the amended section 322 with the narrow literalism petitioner advocates would produce an absurd result, one wholly unwarranted by the legislative history. As between reading the reference to payment for the transportation of mail out of the section altogether, on the one hand, or reading the term "tariffs" in the definition of "overcharges" broadly as including the analogous form of schedule governing rates for the transportation of mail, i.e., outstanding mail-rate orders of the Board and Interstate Commerce Commission, we submit that the latter construction better accords with the expressed Congressional purposes.

The foregoing shows, we submit, that this case is completely governed by Mohawk. As in that case, petitioner's remedy lies not

^{26/} See H. Rep. No. 2346, 85th Cong., 2d Sess., p. 5. The government's practice of using the offset procedure to test the legality of a rate, otherwise correctly applied, forced the affected carrier to resort to both the Court of Claims (as having sole jurisdiction to award money judgment against the United States) and the Interstate Commerce Commission (as having sole jurisdiction to determine the legality of the rate). The complexities of this remedy are illustrated by Pennsylvania R. Co. v. United States, 363 U.S. 202 (1960). Congress wanted the government itself to initiate action before the Commission in such cases, as a private shipper would have to.

here but in the Court of Claims.

II. The Board's treatment of petitioner's investment tax credit was required both by the outstanding final subsidy rate order and by section 406 of the Federal Aviation Act, UNLESS Congress is held to have retroactively amended both the rate order and the Federal Aviation Act

As previously shown, the Board's action here challenged did not fix mail rates or determine subsidy "need" under section 406 of the Act (infra, p. 52), but simply applied the express terms of the outstanding Class Rate I order, 34 C.A.B. 247, to the financial results of petitioner's 1962 operations. We subsequently show that, since the Class Rate I order was final, the Board's power with respect to petitioner's 1962 subsidy was strictly limited to interpreting and applying it in accordance with its original intent and purpose, and that the treatment which the Board has here accorded to petitioner's investment tax credit was plainly required by its profit-sharing provisions. We show, furthermore, that this treatment was likewise mandatory under section 406 of the Federal Aviation Act, which precludes subsidy payments in excess of a carrier's "need", and that

27/ A further objection to review by this Court of profit-sharing refund determinations under the class rate orders lies in the absence of a proper appellate record. See United Gas Pipe Line Co. v. Federal Power Comm'n, 86 U.S. App. D.C. 314, 181 F.2d 796, 799 (1950), cert. denied, 340 U.S. 827; Arrow Airways v. Civil Aeronautics Board, 87 U.S. App. D.C. 71, 182 F.2d 705 (1950); Division of Production v. Halaby, 307 F.2d 363 (C.A. 5, 1962). Here the absence of a proper record relating to factual issues is not critical, but only because petitioner has chosen to confine its appeal to a single, purely legal issue. Most profit-sharing cases would certainly turn largely on issues of fact, or mixed law and fact; see, for instance, the expense disallowances made in paragraphs 5 and 7 of Order E-21663 (Tr. 276), which petitioner contested up to the final Board level (Tr. 263-6). For an elaboration of this point, we respectfully refer the Court to pages 16-20 of our brief in the Mohawk case (No. 17,986, Brief for Respondent).

section 203(e) of the Revenue Act of 1964 (infra, p. 56-7) did not have the effect of amending either section 406 or the outstanding Class Rate I order.

A. The outstanding class rate order embodied the Board's "actual tax" policy

As we have already pointed out (supra, p. 14), the Class Rate I order was final as to the year 1962. Since that order was not appealed within 60 days of its adoption, and since it was not reopened prior to January 1, 1963 by an appropriate carrier petition or Board order, the Board was subsequently without power to amend retroactively any of the provisions of that order, directly or by "interpretation". Transcontinental & Western Air v. Civil Aeronautics Board, 336 U.S. 601 (1949).

On the contrary, in determining petitioner's 1962 profit-sharing refund, the Board was strictly bound by the terms of that order -- and so is petitioner.

That the profit-sharing provisions of the Class Rate I order were intended to embody, and did embody, the Board's historic "actual tax" policy is hardly open to serious question. That order makes each carrier's annual earnings after applicable income taxes subject to profit-sharing, and provides that:

"F. Income taxes. -- Federal and State income taxes shall be determined on the basis of the carrier's income tax returns for each year as submitted to the taxing authorities, with such amendments or revisions . . . as may have been filed as of the date of the final determination of excess profits . . . under this order . . ." (34 C.A.B. at 426)

The foregoing language is simply a paraphrase of the Board's
28/ language in the Western-Inland case, where the "actual tax" or

28/ Western Air Lines and Inland Air Lines, Mail Rates, 14 C.A.B. 201, 243 (1951).

"tax return" policy in subsidy determinations was described as follows (14 C.A.B. at 251 n.):

"By the tax return method in past period mail rate cases we mean the technique of providing for a carrier's liability for income taxes on the basis of reliable evidence regarding the carrier's tax returns filed with the Bureau of Internal Revenue, together with any adjustments made by the Bureau as of the most recent practicable date prior to the Board's order establishing final mail rates."

In Western-Inland the Board rejected various alternative methods of allowing for taxes in subsidy cases, on the grounds that these methods tended to provide an allowance for taxes in excess of the carrier's actual tax liability. The Board said (14 C.A.B. at 252):

"Inquiry into the purpose underlying the income tax allowance readily demonstrates why we consider the [other proposed] methods unsuitable. Mail rates for domestic carriers for past periods are generally established in amounts which meet the carrier's 'need', under honest, economical, and efficient management, and also provide a 7 percent return on the recognized investment. These two amounts together constitute the fair and reasonable rate of mail compensation required by section 406(b) of the Act. A third amount is also provided to cover federal income taxes on the theory that if the carrier must pay taxes on the profit included in the mail rate, it will not, in fact, receive the fair and reasonable rate to which it is entitled. Therefore, as we see it, the function of the federal income tax allowance is to insure that the carrier receives this compensation as if it were a cost of doing business. On the other hand, this allowance is not designed to guarantee that the carrier will receive a gratuity or bonus which it can use to offset other losses. An allowance greater than the actual tax liability affords such a gratuity and should be avoided if possible." (emphasis added) 29/

The Board's "actual tax" policy was upheld by this Court in Summerfield v. Civil Aeronautics Board, 92 U.S. App. D.C. 248,

29/ The Board acknowledged that it had previously used a "constructive tax" method, which had been simpler to administer; but it observed that this was the first case in which it had been definitely demonstrated and called to its attention that this method awarded the carrier an allowance for taxes which had not been and would not be actually required for that purpose (14 C.A.B. at 251).

207 F.2d 200, 206 (1953), aff'd sub nom. Western Air Lines v. Civil Aeronautics Board, 347 U.S. 67 (1954), and thereafter had been undeviatingly followed by the Board in subsidy cases. In two instances prior to this, moreover, the Board has applied its "actual tax" policy to tax reductions resulting from "incentive" provisions of the tax laws somewhat similar to the investment credit. In the Transatlantic Final Mail Rate Case, 21 C.A.B. 484, 520, 522-5 (1955), the Board rejected the argument that tax reductions resulting from the "accelerated amortization" provisions of section 168 of the 1954 Internal Revenue Code, 26 U.S.C. 168, should not be taken into account in subsidy computations.^{30/} In the Reopened Pan American Mail Rate Case, 35 C.A.B. 540, 555 (1962), the Board took the same position with respect to tax reductions resulting from the "liberalized depreciation" provisions of section 167 of the 1954 Internal Revenue Code, 26 U.S.C. 167.^{31/}

30/ This decision was set aside in Trans World Airlines v. Civil Aeronautics Board, 102 U.S. App. D.C. 391, 254 F.2d 90 (1958), not on the merits but because of a procedural error. On remand, the Board readopted its earlier conclusion on this issue. Reopened Transatlantic Final Mail Rate Case, Order E-22022 (April 12, 1965), pp. 37-47.

31/ Moreover, in two previous individual-carrier subsidy rate cases and in a prior profit-sharing determination under Class Rate I the Board has applied its "actual tax" policy, as it did here, to the investment tax credit. Alaska Coastal-Ellis Airlines, Mail Rates, Orders E-20790 and E-20835 (May 5 and 19, 1964); Aloha Airlines, Subsidy Mail Rates, Orders E-21138 and E-21179 (July 30 and August 11, 1964); Bonanza Air Lines, Subsidy Refund - 1962, Order E-21137 (July 30, 1964). The issue was further extensively discussed and the same conclusion reached in Local Service Class Subsidy Rate Investigation (Class Rate III), Order E-21227 (August 28, 1964), pp. 32-36 (infra, p. 61-4), which governs the subsidy rates of petitioner and the other local-service carriers from July 1, 1964, forward. None of these orders, we note, has been appealed.

Thus it is clear both from the language of the Class Rate I order, and from ten years of undeviating precedent prior to (as well as since) its adoption, that the Board's "actual tax" policy was intended to govern the computation of income taxes for profit-sharing purposes under that order, and that tax reductions resulting from subsequent changes in the tax laws would accordingly increase after-tax profits to be shared between the carriers and the government.

Petitioner's contention (Br. 42-3) that the "actual tax" policy was not embodied in the Class Rate I order is based primarily on that order's use of the phrase "after applicable income taxes". The evident purpose for using the word "applicable", however, was to make it clear that only taxes relating to the year in question are to be taken into account in the profit-sharing computation for that year. Here, petitioner proposes to take into account \$25,660 in taxes which are not only not "applicable" but totally non-existent, since petitioner has not paid them and never will.

Nor can the conclusion sought by petitioner be drawn from the fact that the subsequent Class Rate III order specifically mentions the investment tax credit, whereas the Class Rate I order (adopted long before the credit was enacted) does not. The Board made it perfectly clear in the Class Rate III order that no change of policy as to the investment tax credit was intended (Order E-21227, p. 32):

"The profit-sharing provisions of Class Rate III relating to income tax are based on the Board's 'actual tax' policy which was first established in the 1951 Western-Inland Case, and which has been applied unswervingly by the Board since that time in both individual subsidy rate cases and the prior class rates. The application of this principle will be the same under the new class rate as it was under prior class rates. However, for the purposes

of clarity and to resolve certain areas of misunderstanding which have arisen under Class Rate II, some language changes have been made. Generally the trouble areas . . . involve (1) investment tax credit . . ." (emphasis added) 32/

In short, none of petitioner's arguments in any way impeaches the Board's consistent interpretation of its own order as embodying the "actual tax" policy -- an interpretation which, as ample authority attests, is entitled to "great weight" in the courts. Udall v. Tallman, 380 U.S. 1, 16 (1965); Outland v. Civil Aeronautics Board, 109 U.S. App. D.C. 90, 284 F.2d 224, 228-9 (1960).

B. The Board's "actual tax" policy is a necessary corollary of the "need" standard of section 406(b)(3) of the Federal Aviation Act

Petitioner argues that the "actual tax" policy is not mandated by section 406(b)(3) of the Federal Aviation Act (infra, p. 52), but is the Board's own creation, which the Board has been free to abandon at any time. Accordingly, it argues, there is no incompatibility between section 203(e) of the 1964 Revenue Act (infra, p. 56-7) and section 406; the sole incompatibility is between the cited tax provision 33/ and a policy which the Board has chosen in its discretion to adopt.

32/ Nor does the phrase "(including tax carryback and carry-forward credits)" in Class Rate I imply an intent to exclude other credits in computing the tax allowance, as petitioner suggests. The quoted phrase (34 C.A.B. at 426) modifies not "taxes" but "amendments or revisions", which obviously does not apply to credits relating to the current year claimed on the original tax return. The evident purpose of the quoted reference is to deal with the crediting of one year's overpayment against another year's tax liability.

33/ The purpose of this contention, of course, is to break the force of the Board's argument that repeals or amendments of statutory provisions by implication are not favored (see infra, p. 28).

It is true that, prior to the Western-Inland Mail Rate Case,
14 C.A.B. 201, 243, 251-5 (1951), the Board followed not the "actual
tax" but a "constructive tax" policy in past-period subsidy cases.
At the time, the Board undoubtedly thought that the adoption of the
new policy was a matter of its discretion, not of legal necessity.^{34/}
However, the very cases in which the Board's adoption of the "actual
tax" policy was affirmed laid down an interpretation of section 406
which made it clear why the Board thereafter had no choice but to
follow the "actual tax" policy in past-period subsidy cases.^{35/} In
the Delta case, 347 U.S. at 79, the Supreme Court held that under
section 406(b)(3) a carrier's "need" is not merely a factor to be
taken into consideration, but sets an upper limit on the subsidy which
the Board is authorized to pay. In the companion Western case, 347
U.S. at 71, the Supreme Court held that in determining a carrier's
"need" its revenues from all sources must be taken into account:

^{34/} For the Board's statement of its reasons for adopting the
"actual tax" policy, see supra, p. 22.

^{35/} Summerfield v. Civil Aeronautics Board, 92 U.S. App. D.C. 248, 207 F.2d 200 (1953), aff'd sub nom. Western Air Lines v. Civil Aeronautics Board, 347 U.S. 67 (1954); Summerfield v. Civil Aeronautics Board, 92 U.S. App. D.C. 256, 207 F.2d 207 (1953), aff'd sub nom. Delta Air Lines v. Summerfield, 347 U.S. 74 (1954); and see American Overseas Airlines v. Civil Aeronautics Board, 103 U.S. App. D.C. 41, 254 F.2d 744 (1958). These cases all involved subsidy determinations for past periods, made when the facts of the carriers' operations for the periods in question were fully known. While Class Rate I was a prospective rate order, its profit-sharing provisions, like a past-period rate order, operated on the known facts of each year's operations, including actual tax payments as adjusted to the date of final profit-sharing determination. There is accordingly no present necessity to discuss the applicability of the cited cases or the "actual tax" policy to purely prospective subsidy determinations, or to the profit-sharing treatment of tax adjustments subsequent to the date of final refund determination.

"If the carrier's treasury is lush, 'the need' for subsidy decreases whether the opulence is due to transportation activities or activities incidental thereto."

The Western and Delta cases held that a carrier's "need" for subsidy is reduced by its revenues from non-transport activities; by its gain on the sale of part of its route; and by any profits in excess of a fair return earned by another of its divisions, even if that division is not itself receiving subsidy.^{36/} The carrier, in other words, requires certain funds to accomplish the goals of the Act, i.e., "to maintain and continue the development of air transportation". If those funds are available to the carrier from any source other than subsidy, then there is no "need" for them to be supplied from subsidy, and the Board is not authorized to do so. This principle is obviously applicable to funds supplied by tax reductions, whatever the motive of the taxing power in enacting such reductions. If, for example, a carrier prior to a particular tax reduction has a "need" for \$10,000,000 in annual subsidy to enable it to accomplish the purposes of the Act, and the tax laws are then so amended as to reduce its tax bill by \$1,000,000 a year, its annual subsidy "need" is now plainly only \$9,000,000, and in the absence of an amendment to section 406 the Board is without authority to continue paying it \$10,000,000.^{37/}

36/ See also Northwest Airlines v. Civil Aeronautics Board, U.S. App. D.C. 340 F.2d 789 (1964).

37/ The foregoing discussion discloses the fallacy of petitioner's suggestion that the Board could reconcile section 203(e) and section 406 by the simple expedient of declaring that the carriers have a "need" for a tax allowance in excess of the taxes they actually pay -- quite aside from the fact that the Board in the order under review was not determining petitioner's "need" but simply applying the terms of the Class Rate I order. The sole purpose of the (footnote continued)

Accordingly, the issue in this case is not whether section 203(e) of the Revenue Act of 1964 overrides one of the Board's policies, but whether Congress has set aside the "need" and "all other revenue" limitations on the Board's authority to pay subsidy heretofore imposed by section 406(b)(3) of the Federal Aviation Act -- and whether, moreover, it has done so not merely prospectively, so as to govern subsidy rate orders entered after the effective date of section 203(e), but retroactively, so as to amend subsidy rate orders which on that date had long since become final.

III. Section 203(e) of the Revenue Act of 1964 should not be interpreted as amending section 406 of the Federal Aviation Act

Nothing in the 1962 or 1964 Revenue Acts explicitly amends section 406 of the Federal Aviation Act, and it is a basic principle of statutory construction that repeals or amendments of prior statutes by implication are not favored.^{38/} It is significant, in this connection, tax allowance is to insure that the carriers actually receive the rate of return on their investment which the Board has found will enable them to attract capital and thus continue the development of air transportation. If the carriers' need to make up operating losses ("break-even need"), their need for a rate of return sufficient to attract capital investment, and their need for reimbursement of the taxes they actually pay are all met, there is no possible basis on which the Board could find that they "need" an additional tax allowance representing taxes neither paid nor payable. See Western-Inland Mail Rate Case, 14 C.A.B. 201, 243, 252 (1951); Transatlantic Final Mail Rate Case, Reopened, 23 C.A.B. 307, 320 (1956).

^{38/} United States v. Burroughs, 289 U.S. 159, 164 (1933); City of Tulsa v. Midland Valley R. Co., 168 F.2d 252, 254 (C.A. 10, 1948); United States v. 24 Cans Containing Butter, 148 F.2d 365, 367 (C.A. 5, 1945), cert. denied, 326 U.S. 752; 1 Sutherland, Statutory Construction § 1913 (3d ed. 1943). Moreover, where a later general statute (such as section 203(e)) appears to conflict with an earlier specific one comprehensively dealing with a particular subject matter or class of persons (such as section 406), the presumption ordinarily is that the specific statute is intended to remain in effect as an exception to the general (footnote continued)

that on the one prior occasion when Congress desired to have the Board exclude from its subsidy calculations an item which otherwise would have been included under the "need" and "all other revenue" standards of section 406(b)(3), it did so by specifically amending section 406.^{39/}

Nevertheless, such repeal or amendment is possible, if the language of the later statute plainly so requires, or if its legislative history clearly demonstrates that such repeal or amendment was intended, or if the evident purpose of the later statute will otherwise be frustrated. As we now show, however, none of these conditions is present here.

- A. The language of section 203(e) does not cover subsidy determinations such as those made by the Board under section 406

The Board does not suggest that it must be specifically named in a statute before that statute is held to affect its functions. It does suggest, however, that where as here a general statute is plainly designed to govern one particular type of program in which a number of agencies engage, and where the Board administers another program which, although historically linked to the first, is quite different in its underlying purpose, techniques, and principles, the general statute should not be assumed to apply to the Board's unique program, absent definite indication that Congress so intended.

one. Rodgers v. United States, 185 U.S. 83, 87-8 (1902); Bulova Watch Co. v. United States, 365 U.S. 753, 758 (1961); Panama Canal Co. v. Anderson, 312 F.2d 98, 100 (C.A. 5, 1963), cert. denied, 375 U.S. 832; 1 Sutherland, op. cit. supra, § 2021.

^{39/} This was the so-called "capital gains" provision, P.L. 85-373, 72 Stat. 84 (1958), which became section 406(d) of the Federal Aviation Act of 1958 (infra, p. 53), providing in essence that gains from the sale of flight equipment should not be treated as "other revenue" if promptly reinvested in other flight equipment. See the Capital Gains Proceeding, 27 C.A.B. 79, 81 (1958).

Section 203(e) of the 1964 Revenue Act (infra, p. 56-7) is concededly designed to govern the actions of all federal regulatory agencies, including the Board, in cases where such agencies are setting rates for regulated enterprises subject to their jurisdiction, and such rate determinations are based on the enterprises' "cost of service". Petitioner argues that subsidy is paid out under "rates", which at least formally represent compensation for the transportation of mail, and which are based in part on the subsidized carriers' "cost of service"; hence, it argues, section 203(e) is directly applicable on its face to subsidy determinations.

However, despite the similarities between subsidy and commercial ratemaking which petitioner points out, the differences are far more fundamental. Ordinary commercial ratemaking deals with the price which the users of a regulated service pay for it; its basic underlying assumption is that, in the absence of regulation, the users of the service would probably be called on to pay too much. Subsidy ratemaking under section 406(b)(3) of the Federal Aviation Act, on the other hand, deals with that portion of the cost of air service which the users of that service do not pay; its underlying assumption is that the subsidized carriers cannot charge their customers enough to pay for the quantity and quality of air service which Congress con-
40/
siders to be in the public interest. In this sense, subsidy

40/ The foregoing discussion points up the speciousness of petitioner's argument (Pet. Br. 39) that the Board's "actual tax" treatment of the investment credit in subsidy cases would nullify the effects of the treatment required by section 203(e) in commercial rate cases affecting subsidized carriers. This argument would make sense only if a ceiling were being imposed on such carriers' commercial rates to keep them from earning more than a fair rate of return.
(footnote continued)

determination is the antithesis of commercial maximum-rate regulation. The Board's function, in fact, is essentially promotional rather than regulatory.

In subsidy matters, the government in no sense occupies the role of a customer. The sole connection between subsidy and transportation of the mail is in the matter of eligibility; otherwise, a carrier's subsidy is in no way dependent on the quantity of mail it carries, or indeed on the actual carriage of any mail at all. Compensation for actual carriage of mail is rendered entirely through service mail pay,^{41/} which is fixed on a wholly different basis, in different proceedings. The government is not buying air transportation with its subsidy, as petitioner suggests; it is underwriting the operations of the carriers so that they can make air transportation available to the public at rates the public is able and willing to pay.

Some features of ordinary utility rate regulation (particularly procedural ones) have of course been carried over to the Board's subsidy determinations under section 406(b)(3), either by statutory

In reality, however, such carriers' rates are limited by what their customers are able and willing to pay, by competition with other forms of transportation, and to some extent by the general air rate structure; by definition, they are unable to charge enough to earn a fair rate of return, with or without the investment tax credit.

^{41/} The subsidy formula of Class Rate I, for example, contains no factor relating to the quantity of mail carried; nor have other subsidy rates contained such factors for many years. Compare Domestic Trunklines, Service Mail Rates, 21 C.A.B. 8 (1955) (service mail rates scaled to ton-miles and pounds of mail emplaned). Service and subsidy rates have been separately determined since prior to Reorganization Plan No. 10 of 1953, 67 Stat. 644, 5 U.S.C. 133z, which separated the disbursing functions as to the two types of rates.

42/ command or because the Board has found them appropriate. 43/ But these carryovers do not show that subsidy determination and commercial rate regulation are essentially the same; they show only that one of the objects of both is to encourage the highest level of managerial efficiency and that the same techniques will frequently be as effective in one field as in the other.

44/ On the other hand, the results of the Western and Delta cases show that where the "need" and "all other revenue" limitations on subsidy under section 406(b)(3) conflict with ordinary utility rate-making principles, the former prevail and the latter give way. Thus, where a regulated utility has several divisions, ordinary utility rate principles require the customers of each division to pay the operating and capital costs of that division and no more; rates in one division are not reduced because of excess earnings in another. Yet that is just what the Court required with respect to subsidy in the Delta case. Similarly, it would not be customary under ordinary utility rate principles to reduce rates by the amount of an unplanned and non-recurring

42/ E.g., the rate finality principle, Transcontinental & Western Air v. Civil Aeronautics Board, 336 U.S. 601 (1949), and the "honest, economical and efficient management" standard, see American Overseas Airlines v. Civil Aeronautics Board, 103 U.S. App. D.C. 41, 254 F.2d 744 (1958).

43/ E.g., the regulation of depreciation charges, see Northwest Airlines v. Civil Aeronautics Board, ___ U.S. App. D.C. ___, 340 F.2d 789, 790-1 (1964), and the disallowance of such non-transport expenditures as lobbying expenses, charitable contributions, and the like, see the Class Rate I order, para. 3, 34 C.A.B. at 423.

44/ Western Air Lines v. Civil Aeronautics Board, 347 U.S. 67 (1954), aff'g 92 U.S. App. D.C. 248, 207 F.2d 200 (1953); Delta Air Lines v. Summerfield, 347 U.S. 74 (1954), aff'g 92 U.S. App. D.C. 256, 207 F.2d 207 (1953).

gain on the sale of part of the utility's system; yet this is just
what the Court required with respect to subsidy in the Western case.
^{45/}

Moreover, the Board has frequently applied different principles in subsidy cases than in commercial rate cases. Thus the Board has in subsidy cases applied the "actual tax" policy to tax savings resulting from increased amortization and depreciation deductions under sections 167 and 168 of the Internal Revenue Code, 26 U.S.C. 167, 168; whereas in the General Passenger Fare Investigation, 32 C.A.B. 291, 326 (1960), the Board ruled that such tax savings would not be taken into account in commercial rate cases (see supra, p. 23). Similarly, the Board has frequently provided for a different rate of return in subsidy cases than it has in commercial rate cases, and sometimes for a different depreciation allowance as well. These differences of treatment were upheld in Northwest Airlines v. Civil Aeronautics Board, ___ U.S. App. D.C. ___, 340 F.2d 789, 791-2 (1964), where two of the carrier's complaints were precisely the Board's failure to allow its domestic division the same depreciation allowance and rate of return for subsidy "offset" purposes as had been allowed for passenger fare purposes in the General Passenger Fare Investigation, supra.

The term "cost of service" has become a term of art in the field of utility and carrier rate regulation. By using that term in section 203(e), Congress presumably intended to draw on the connotations which have attached to that term over the years -- notably, the connotation

^{45/} This Court's decision in American Overseas Airlines v. Civil Aeronautics Board, 103 U.S. App. D.C. 41, 254 F.2d 744 (1958) further illustrates the differences between subsidy and commercial rate cases.

that a regulated utility's or carrier's customers are expected to pay its cost of serving them. In the case of a subsidized air carrier, however, the customers do not pay the cost of the carrier's service to them, but only part of it; the unpaid balance becomes the principal element of the carrier's "need" for subsidy.

"Need", the central concept in subsidy determinations, is related to "cost of service" but by no means identical with it. A carrier always has a "cost of service", but it may or may not have a "need".

^{46/} "Need", as pointed out by Judge Prettyman in the Western case, is not to be conceived as a sum from which deductions are made, but as a net amount, namely the amount which will make up the carrier's operating losses and will (after taking into account its revenues from other sources) give it an after-tax rate of return on investment sufficient to attract the capital it needs to expand and develop.

The Board in determining "need" is not mediating between the carriers and their customers, but is promoting a public service which is not now, but may some day be, self-supporting.

All of the foregoing considerations demonstrate, we submit, that a statute expressly directed to "cost of service" determinations in a context of regulation cannot automatically be presumed to apply to "need" determinations in a context of promotion and subsidy. Certainly it cannot be said that "an intent to repeal, modify, or supersede the former Act [here, section 406] . . . is manifestly clear from the context of the legislation [here, section 203(e)]." City of Tulsa v. Midland Valley R. Co., 168 F.2d 252, 254 (C.A. 10, 1948).

^{46/} Summerfield v. Civil Aeronautics Board, 92 U.S. App. D.C. 248, 207 F.2d 200, 206 (1953), aff'd sub nom. Western Air Lines v. Civil Aeronautics Board, 347 U.S. 67 (1954).

- B. The legislative history of section 203(e) shows that Congress was exclusively concerned with preventing regulatory agencies from requiring that the benefit of the investment tax credit "flow through" to utility customers in commercial rate cases

Petitioner concedes (Br. 37-8) that "much" of the legislative history of section 203(e) is concerned with whether regulatory agencies should be permitted to require the benefit of the investment tax credit to "flow through" to the customers of regulated utilities. We assert, on the contrary, that substantially all of the legislative history is concerned with this issue, and that nothing in that history gives the slightest indication that Congress ever considered the applicability of section 203(e) to subsidy determinations such as those the Board makes under section 406(b)(3).

Section 203(e)'s limited purpose clearly appears from the committee reports accompanying the 1964 Revenue Act. Thus, the House Committee Report summarized the bill's effect on the investment credit as follows:

47/

"2. Investment credit -- In the case of the investment credit, the bill . . . (b) prevents regulatory commissions in certain cases from requiring the "flow through" of the benefits of the investment credit to the customers of regulated industries; and (c) makes other revisions in the investment credit." (emphasis added.)

A provision to control agency action in commercial rate cases was believed necessary because of the adoption by the Federal Communications Commission and Federal Power Commission of a "policy that

47/ H. R. Rep. No. 749, 1964-1 U.S. Code Cong. & Ad. News 1313-4; see, also, S. Rep. No. 830, ibid. at 1674.

benefits from the investment credit made available by the Revenue Act
^{48/}
of 1962 should 'flow through' immediately to the customers."

"As indicated above in the case of the public utility property Congress is merely directing the federal regulatory agencies not to 'flow' the benefits of the investment credit 'through' to the customers over any period shorter than the usable lives of the property involved. In the case of the other property Congress is directing the federal regulatory agencies not to 'flow' this benefit 'through' at any time." (emphasis added)^{49/}

Nowhere do the committee reports advert to the possible application of section 203(e) to subsidy determinations by the Board under section 406 or to any other type of subsidy situation.

The floor debates on section 203(e) strengthen the impression that Congress' sole purpose was to prevent the compulsory "flow through" of the investment tax credit to the customers of regulated utilities. As the portions of the debates quoted by petitioners (Br. 20-25) clearly show, both the supporters and opponents of the measure spoke exclusively in terms of regulated (not subsidized) industries, and in terms of the conflict between the interests of the regulated utilities and their customers. ^{50/} Dozens of additional citations ^{51/} to the debates could be given, all to the same effect.

48/ ibid. at 1344, 1714.

49/ ibid. at 1347, 1717; and see the minority views of Senators Douglas, Ribicoff, and Gore, ibid. at 1840, 1842, 1865.

50/ Petitioner's citations from the legislative history of the original investment tax credit itself, and of Congressional reaction to agency decisions relating to that credit, similarly show an exclusive concern with the "flow through" of the credit to customers, and an absence of any reference to subsidy determinations.

51/ See 110 Cong. Rec. 1284, 1292, 1297, 1354-65, 1441-53, 1502, 1883-89, 2038-42, 2049-84, 2128-9, 2199-2205, 2356, 2390, 3564.

The effect of section 203(e) on the airline industry was virtually never mentioned during the debates.^{52/} On the few occasions when the Civil Aeronautics Board was mentioned, it was only with regard to its regulatory, never its subsidy-determining functions. The only really significant references to the Board were made by Senator Long of Louisiana, who was the floor manager of the bill and whose remarks are therefore particularly significant:

"While it may have the power to do so, the Civil Aeronautics Board does not regulate the rates of the airlines. The airlines enjoy the full benefit of the 7 percent tax credit." (110 Cong. Rec. 1502)

And subsequently, in response to a question:

"So far as the C.A.B. is concerned, that regulatory agency does not fix the rates of the airlines, those rates are fixed by competition. Therefore, so far as that agency is concerned, this does not make any difference. So there is no real reason why that agency should become involved one way or the other."
(110 Cong. Rec. 2061)

These remarks make sense in the context of commercial rate regulation, since it is historically a fact that the Board has had few occasions to exercise its power to fix maximum commercial rates. On the other hand, Senator Long's remarks are inexplicable in the context of subsidy determinations: subsidy is not in any sense fixed by competition, but is always and invariably fixed by the Board--a fact well known to Congress, since the Board must return each year for

^{52/} The sole references to the airlines and/or the Board we have found are as follows: 110 Cong. Rec. 1357, 1502, 2056, 2061, 2063, 2067-8, 2084.

subsidy appropriations. Senator Long's remarks clearly show, we submit, that commercial rate regulation was the sole topic on his mind; it is inconceivable that he would have made them if he had had any idea of section 203(e) applying to subsidy cases.

In Panhandle Eastern PipeLine Co. v. Federal Power Comm'n, 115 U.S. App. D.C. 8, 316 F. 2d 659 (1963), cert. denied, 375 U.S. 881, this Court sitting en banc refused to hold that Congress, in enacting the "liberalized depreciation" provisions of section 167 of the Internal Revenue Code, 26 U.S.C. 167, had impliedly amended the rate-making provisions of the Natural Gas Act. This Court said (316 F.2d at 662):

"Nothing in the language or legislative history indicates that Congress considered [the tax provision's] regulatory consequences. Thus to infer that the statute materially altered fundamental principles of rate regulation . . . it must clearly appear that Congress intended to benefit producers to the exclusion of consumers. It does not so appear . . ." (emphasis added)

We submit that the Panhandle decision supports the Board's position here. In section 203(e), it is true, Congress has expressed a clear intention to alter the principles of rate regulation applicable to commercial rate cases, and to benefit producers to the exclusion of

53/ The opponents of section 203(e) denounced it as "ordering the regulatory agencies to cheat the consumer". (Senator Gore, 110 Cong. Rec. 1292) It seems incredible, if they had had any intimation that section 203(e) was intended to apply to subsidy determinations, that they would not equally have denounced the provision as cheating the taxpayers by duplicating the bounty already granted to the airlines under section 406; yet nowhere in the debates was any such criticism made.

54/ The court limited the apparently contrary holding of City of Detroit v. Federal Power Commission, 97 U.S. App. D.C. 260, 230 F.2d 810 (1956), cert. denied, 352 U.S. 829, to its particular facts.

consumers, by forbidding regulatory agencies to "flow through" the benefits of the investment tax credit to consumers. It has not, however, indicated any intent whatever to alter the principles of subsidy determination applied by the Board under section 406(b)(3) -- quite a different matter, as we have seen -- nor has it shown an intent to give subsidized airlines a double gratuity at the expense of the taxpayers. Certainly it cannot be said that such an intent "clearly appears".

C. Fulfillment of the purposes of section 203(e) does not require setting aside the "need" limitation of section 406

Petitioner makes an extended argument that the Congressional purpose in enacting the investment tax credit will be frustrated if the Board's "actual tax" treatment of that credit for profit-sharing purposes under Class Rate I is allowed to stand. Like many of petitioner's other arguments, this one is based on a misconception of the Board's action, of section 406, and of section 203(e).

In the first place, it is a semantic fallacy to suggest, as petitioner does, that the Board here is "taking away" its investment tax credit. As the Supreme Court pointed out in Western Air Lines v. Civil Aeronautics Board, 347 U.S. 67, 73-4 (1954), and as this Court pointed out in Northwest Airlines v. Civil Aeronautics Board, ___ U.S. App. D.C. ___, 340 F.2d 789, 792 (1964), there is no question of "recapture" involved. Petitioner keeps the full amount of its investment tax credit; the sole issue here is whether petitioner shall receive additional money in the form of subsidy to compensate it for taxes which it does not in fact have to pay. In other words, the

question is whether the Congress intended by enactment of section 203(e) to require that the Board grant subsidy pursuant to section 406 in excess of the carriers' "need".

Petitioner insists that Congress so intended. It says that, even though the Board did not take away the investment credit, the net result of the Board's action is to leave petitioner no better off financially than before the credit was enacted, and that this result will frustrate the Congressional purpose. There is no doubt that the investment credit had in it more of an element of bounty or subsidy than the usual tax-code provision; and, under section 203(e), it is plain that, as between regulated utilities and carriers on the one hand and their customers on the other, Congress intended the benefit of this bounty to remain with the former. But as previously pointed out, the government, in relation to subsidy disbursement, does not occupy the position of a customer of the airlines, and it by no means follows that Congress intended to confer duplicate bounties on those already being subsidized out of public funds. We submit that if Congress had intended to confer on petitioner and the other subsidized airlines a double portion of the taxpayers' funds, it would have made its intention plain.

Petitioner, however, argues that the purposes of the investment credit and subsidy under section 406 are different, so that it is plausible that Congress wanted subsidized air carriers to have both benefits, each undiminished by the other. This argument flies in the face of the language of both section 203(e) and section 406.

The former states that the purpose of the investment credit was "to provide an incentive for modernization and growth of private industry", while the latter requires the Board to base a carrier's subsidy on its need for funds --

"sufficient . . . to enable such air carrier . . . to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

Petitioner does not dispute that these stated purposes overlap, and indeed it is plain that, as applied to subsidized air carriers, the objectives of section 406 are more comprehensive than those of section 203(e). Petitioner's attempts to show wherein section 203(e)'s purposes will not be met under section 406 are uniformly without merit.

(1) Petitioner's suggestion (Br. 34) that the Board cannot take into account the incentives required to motivate the particular carrier or carriers whose subsidy rate is being fixed to fulfill the above-quoted objectives of section 406, is refuted by the Supreme Court's discussion of such incentives in Transcontinental & Western Air v. Civil Aeronautics Board, 336 U.S. 601, 606-7 (1949), as well as by the Board's similar discussions in the Class Rate I order itself, 34 C.A.B. 416, 430-2; in the Reopened Transatlantic Final Mail Rate Case, Order E-22022 (April 12, 1965), pp. 24, 27-8, 33; and elsewhere.^{55/}

(2) Petitioner's criticisms (Br. 32-33) of the rates of return provided by the Board in subsidy cases are wide of the mark. Such

^{55/} Western Air Lines v. Civil Aeronautics Board, 347 U.S. 67 (1954), cited by petitioner as casting doubt on the Board's power to use subsidy to give carriers incentives to modernization and growth, actually holds only that the Board cannot give additional subsidy to one carrier for the purpose of providing incentives to other carriers or the airline industry at large.

rates are in fact set at that level which the Board finds will motivate private investors to provide the funds needed by the carriers to carry out the objectives of section 406, including, of course, modernization and growth through the purchase of new equipment.^{56/} Moreover, if petitioner considered the rates of return fixed by the Board in past or current subsidy cases inadequate, it should have challenged these rates at the time, rather than acquiescing in them as it did.^{57/}

(3) Petitioner complains that in some past instances the Board has not provided adequate incentives to subsidized carriers for equipment modernization. If this were so, it would indicate only that the

56/ Capital Gains Proceeding, 27 C.A.B. 79, 82-6 (1958); American Air., Mail Rates, 3 C.A.B. 323, 333 (1942). In Rate of Return, Local-Service Carriers, 31 C.A.B. 685, 691 (1960), the carriers' need for additional investment capital for these purposes was cited as one of the principal reasons for raising their rate of return.

57/ Petitioner's discussion (Br. 32-3) of the rates of return provided by the Board for subsidized carriers, and its comparison of these rates with those allowed to unsubsidized carriers, are seriously misleading, primarily because they ignore the very different capital structures of these two branches of the airline industry, and the different risks to which they are exposed. As we previously pointed out (supra, p. 4n), the 21.35 percent return on equity capital provided in Class Rate I was derived by adding a 50 percent bonus to the cost of such capital to the "Medium Eight" trunklines. In Class Rate III, the Board reduced the return allowed on equity capital to 16 percent only because it found that capital costs had substantially declined for both the trunkline and the local-service carriers, and the new figure was again derived by adding 50 percent to the observed capital costs of the smaller trunklines. (Order E-21227, pp. 21-23, where the Board also noted the great success which Class Rates I and II had had in increasing equity investment in the local-service carriers.)

Board has not always done its job effectively under section 406,
58/
not that section 406 did not provide for such incentives.

(4) There is no merit whatever to petitioner's contention (Br. 27-8) that the Board's "actual tax" treatment of the investment tax credit creates "competitive inequities". As we have seen, petitioner keeps the full amount of both its commercial revenues and its investment tax credit; the issue here is how much additional subsidy money it shall receive. Every dollar of subsidy, of course, represents a "competitive inequity" in petitioner's favor -- a benefit which it receives and its unsubsidized airline and surface-mode competitors do not.

How much stronger and more comprehensive is the incentive given by subsidy under section 406, than by the investment tax credit, may be seen from the 1962 figures for petitioner itself. Petitioner's subsidy for the year before profit-sharing exceeded \$8,800,000, and even after profit-sharing came to nearly \$8,300,000. Of this, some

58/ In fact, however, petitioner's allegations are baseless. The Board has never discouraged or penalized a subsidized carrier which sought to purchase new equipment that would increase its productive efficiency and reduce its cost of service -- the kind of equipment whose purchase Congress surely had in mind in enacting the investment tax credit and section 203(e). In those instances where the Board has refused to underwrite with subsidy the increased operating expenses or newer and more costly flight equipment, it has been because the Board found that the new equipment desired by the carrier, far from increasing its productivity and lowering operating costs, would raise costs and increase the carrier's break-even need. The Board's actions in these cases have simply served to eliminate a subsidy incentive which the investment tax credit would not give an unsubsidized enterprise in the first place.

\$900,000 (after profit-sharing) represented return on investment, i.e., incentive to invest in productive facilities and equipment. In contrast to this giant incentive, the benefit which petitioner derived from the investment tax credit in 1962 amounted to only \$25,660, or somewhat less than 3 percent of the return element in its subsidy alone. The \$200,000 (Tr. 267, lines 24-25) which represents petitioner's retained share of profit in excess of its "fair and reasonable differentiated rate of return" is nearly 8 times the amount of the investment tax credit.^{59/}

Accordingly, since petitioner has failed to point out any respect in which the objectives of the investment tax credit and section 203(e), as applied to the airline industry, are broader than those of section 406(b)(3), and since modernization and growth through the investment of private capital in new facilities, which the investment credit was intended to promote, are far more massively promoted in the subsidized portion of the airline industry by subsidy under the latter section, there is no basis for interpreting section 203(e) as overriding the "need" limitation of section 406(b)(3).

^{59/} The \$903,816 in profits for 1962 which petitioner keeps after profit-sharing (Tr. 267) represents a return of 12.90 percent on its recognized total investment of \$7,006,292. After providing for a return on debt capital of 5.50 percent, this retained profit gives petitioner's common stockholders a return of 31.45 percent on their equity investment of \$1,994,398. In contrast, the benefit of the investment tax credit represents an additional return of only 0.30 percent on total investment, or 1.03 percent on equity.

IV. Section 203(e) of the 1964 Revenue Act should not be interpreted as retroactively amending the outstanding final subsidy rate order applicable to petitioner's 1962 operations

Even if section 203(e) of the Revenue Act of 1964 were to be interpreted as impliedly amending section 406(b)(3) of the Federal Aviation Act, it would by no means follow that such an implied amendment would affect subsidy payable under an outstanding final rate order. It is axiomatic that statutory amendments are ordinarily prospective in their operation only; it requires a clear and unambiguous expression of Congressional intent before a statute will ^{60/} be interpreted as applying retroactively.

The Supreme Court earlier discerned in section 406 of the Act a Congressional intent to carry over to subsidy rate-making the public-utility principle of rate finality, despite language in section 406(a) which might have been given an opposite interpretation. Transcontinental & Western Air v. Civil Aeronautics Board, 336 U.S. 601, 604 (1949). The Court there discussed the importance of rate finality and its long tradition, and refused to infer a Congressional intent to depart from that principle absent a clear expression of such intent.

An important aspect of the principle of rate finality is that a rate not challenged within the time allowed, and not reopened during the period in question by an appropriate petition or order (as Class Rate I was not during 1962), becomes unchallengeable as to such

^{60/} Claridge Apartments Co. v. Commissioner, 323 U.S. 141, 164 (1944); United States v. St. Louis, S.F. & T. Ry. Co., 270 U.S. 1, 3 (1926); 2 Sutherland, Statutory Construction §2201 (3d ed. 1943).

period even if based on an error of law. Many factors go into making up a rate; a legal error entering into any one of them is not jurisdictional, and does not deprive the rate of its finality as to a past period. Even the argument that the rate is unconstitutionally confiscatory cannot be used to breach the finality of such a rate.

Capital Airlines v. Civil Aeronautics Board, 84 U.S. App. D.C. 176, 171 F.2d 339 (1948), cert. denied, 336 U.S. 961.

While the principle of rate finality is not necessarily binding on Congress, we submit that this Court should be extremely hesitant to find an intent on Congress's part to violate that principle by amending an outstanding final rate order. This is particularly true in view of (1) the Supreme Court's finding in T.W.A., supra, as to the original intent of section 406, (2) Congress's conspicuous ^{61/} refusal to amend section 406 retroactively on a prior occasion, and (3) the total absence of any positive expression of intent to have section 203(e) affect any kind of outstanding rate orders, much less subsidy orders under section 406(b)(3).

Petitioner contends, however, that the Class Rate I order itself was designed to incorporate subsequent changes in the tax laws, includ-
^{62/} ing such provisions as section 203(e). Aside from the fact that

61/ When Congress undertook to amend the "need" standard of section 406(b)(3), by adding the "capital gains" provision now embodied in section 406(d) (see supra, p. 29), it carefully designated as the effective date of its amendment the very date (April 6, 1956) on which the Board had reopened all existing final subsidy rates in order to investigate the capital gains problem. See the Capital Gains Proceeding, 27 C.A.B. 79 (1958).

62/ This is the basis of its argument that the Class Rate I order does not embody the "actual tax" policy, which we have already shown to be fallacious (supra, pp. 21-25).

section 203(e) was not adopted until 1964, this argument is a fallacy. The class rate order was not concerned with the tax laws or amendments thereto as such; it simply treated the taxes payable by a subsidized carrier as an external fact to be taken into consideration in fixing subsidy -- in this instance, in the profit-sharing calculations. Under the "actual tax" policy, as embodied in the class rate order, the taxes to be taken into consideration were those actually paid or payable by the carrier, not some constructive, hypothetical, or otherwise different figure. If the tax payable were reduced, subsidy would also be reduced; it was a matter of indifference under the class rate whether the reduction in tax was the result of a decrease in taxable income, a lowering of the tax rate, or some special provision of the tax laws. It was patently not the intent of the class rate order, however, that the Board in making profit-sharing computations should ignore a reduction in taxes actually paid, as petitioner would have it, whatever the cause of the reduction.

The plain fact of the matter is that petitioner had available a remedy by which it could have earlier challenged the Board's treatment of its investment tax credit -- one which would not have run up against the principle of rate finality -- but elected not to use it. At the time the Class Rate I order was adopted and made final, of course, the issue could not have been raised, since the credit did not yet exist. When the credit was enacted in the fall of 1962, however, petitioner could have filed with the Board a proper petition to reopen the class rate for the purpose of amending the profit-sharing treatment of the credit.

63/ Petitioner must certainly have been well aware that the Class Rate I order embodied the "actual tax" policy, and that the Board would (footnote continued)

If the Board had then refused to reopen the rate or to depart from the "actual tax" treatment of the credit, petitioner could have secured a judicial interpretation of whether or not Congress in enacting the credit had impliedly amended section 406. The question of retroactive amendment of an outstanding final rate order would not have arisen, since the petition to reopen would have converted the balance of 1962 into an "open-rate" period and thus made possible the application to such period of whichever treatment of the investment credit was ultimately held correct, without violation of the finality principle.

Petitioning for a reopening of the rate, however, would have exposed petitioner to the risk that the Board might reconsider other portions of the class rate as well, and might adopt provisions less favorable to petitioner. Petitioner accordingly chose not to thus reopen the rate, but continued to accept its benefits -- including, as we have seen, an after-profit-sharing return of 12.90 percent on overall investment and 31.45 percent on equity. Having done so, petitioner is in no position to argue that the Board's 1962 profit-sharing treatment of its investment tax credit violates the intent of Congress, unless Congress is deemed to have wholly set aside the principle of rate finality.^{64/}

apply that policy to the investment tax credit, in view of the Board's unswerving adherence to that policy, and particularly its application of that policy to earlier "incentive" tax changes (see supra, p. 23). Petitioner must also have been aware that a subsequent profit-sharing determination under Class Rate I would not be an independent rate-making determination, but simply an administrative computation and application of the terms of the Class Rate I order (see supra, pp. 7, 20).

64/ In this connection, it is certainly significant that, when the Board formally incorporated the "actual tax" treatment of the investment tax credit in the Class Rate III order, the affected carriers (including petitioner) chose not to seek judicial review, although neither the principle of rate finality nor the presumption against retroactive legislation would have stood in their path had they done so.

CONCLUSION

For the reasons stated in Part I of this brief, the petition for review should be dismissed for lack of jurisdiction. If the Court reaches the merits, the Board's action should be affirmed.

Respectfully submitted,

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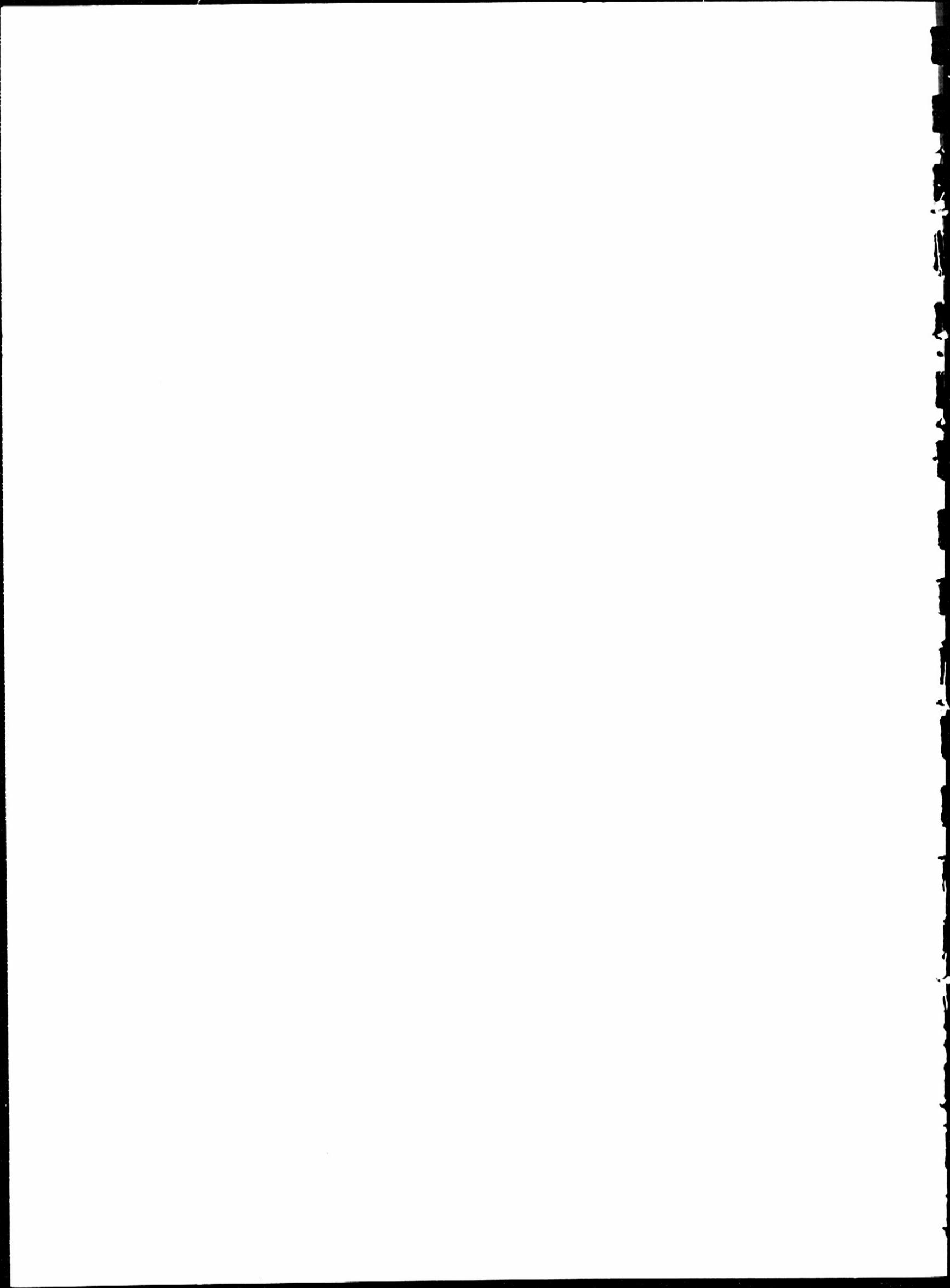
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Dated: September, 1965



APPENDIX A

Statutes Involved

Relevant excerpts from the Federal Aviation Act of 1958 (72 Stat. 731, 49 U.S.C. 1301 et seq.):

* * * * *

TITLE IV--AIR CARRIER ECONOMIC REGULATION

CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

Sec. 401. [72 Stat. 754, as amended by 76 Stat. 143, 49 U.S.C. 1371]

* * * * *

Requirement as to Carriage of Mail

(1) Whenever so authorized by its certificate, any air carrier shall provide necessary and adequate facilities and service for the transportation of mail, and shall transport mail whenever required by the Postmaster General. Such air carrier shall be entitled to receive reasonable compensation therefor as hereinafter provided.

* * * * *

TRANSPORTATION OF MAIL

* * * * *

Sec. 405. [72 Stat. 760, 49 U.S.C. 1375]

* * * * *

Tender of Mail

(d) From and after the issuance of any certificate authorizing the transportation of mail by aircraft, the Postmaster General shall tender mail to the holder thereof, to the extent required by the Postal Service, for transportation between the points named in such certificate for the transportation of mail, and such mail shall be transported by the air carrier holding such certificate in accordance with such rules, regulations, and requirements as may be promulgated by the Postmaster General under this section.

* * * * *

RATES FOR TRANSPORTATION OF MAIL

Authority to Fix Rates

Sec. 406. [72 Stat. 763, as amended by 76 Stat. 145, 49 U.S.C. 1376] (a) The Board is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith (including the transportation of mail by an air carrier by other means than aircraft whenever such transportation is incidental to the transportation of mail by aircraft or is made necessary by conditions of emergency arising from aircraft operation), by each holder of a certificate authorizing the transportation of mail by aircraft, and to make such rates effective from such date as it shall determine to be proper; (2) to prescribe the method or methods, by aircraft-mile, pound-mile, weight, space, or any combination thereof, or otherwise, for ascertaining such rates of compensation for each air carrier or class of air carriers; and (3) to publish the same.

Rate Making Elements

(b) In fixing and determining fair and reasonable rates of compensation under this section, the Board, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the Board shall take into consideration, among other factors, (1) the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; (2) such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and (3) the need of each such air carrier (other than a supplemental air carrier) for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

Payment

(c) The Postmaster General shall make payments out of appropriations for the transportation of mail by aircraft of so much of the total compensation as is fixed and determined by the Board under

this section without regard to clause (3) of subsection (b) of this section. The Board shall make payments of the remainder of the total compensation payable under this section out of appropriations made to the Board for that purpose.

Treatment of Proceeds of Disposition of Certain Property

(d) In determining the need of an air carrier for compensation for the transportation of mail, and such carrier's "other revenue" for the purpose of this section, the Board shall not take into account--

(1) gains derived from the sale or other disposition of flight equipment if (A) the carrier notifies the Board in writing that it has invested or intends to reinvest the gains (less applicable expenses and taxes) derived from such sale or other disposition in flight equipment, and (B) submits evidence in the manner prescribed by the Board that an amount equal to such gains (less applicable expenses and taxes) has been expended for purchase of flight equipment or has been deposited in a special reequipment fund, or

(2) losses sustained from the sale or other disposition of flight equipment.

Any amounts so deposited in a reequipment fund as above provided shall be used solely for investment in flight equipment either through payments on account of the purchase price or construction of flight equipment or in retirement of debt contracted for the purchase or construction of flight equipment, and unless so reinvested within such reasonable time as the Board may prescribe, the carrier shall not have the benefit of this paragraph. Amounts so deposited in the reequipment fund shall not be included as part of the carrier's used and useful investment for purposes of section 406 until expended as provided above: Provided, That the flight equipment in which said gains may be invested shall not include equipment delivered to the carrier prior to April 6, 1956: Provided further, That the provisions of this subsection shall be effective as to all capital gains or losses

realized on and after April 6, 1956, with respect to the sale or other disposition of flight equipment whether or not the Board shall have entered a final order taking account thereof in determining all other revenue of the air carrier.

* * * * *

TITLE IX--PENALTIES

CIVIL PENALTIES

Safety, Economic, and Postal Offenses

Sec. 901. [72 Stat. 783, as amended by 76 Stat. 149, 49 U.S.C. 1471] (a)(1) Any person who violates (A) any provision of title III, IV, V, VI, VII, or XII of this Act, or any rule, regulation, or order issued thereunder, or under section 1002(i), or any term, condition, or limitation of any permit or certificate issued under title IV, or (B) any rule or regulation issued by the Postmaster General under this Act, shall be subject to a civil penalty of not to exceed \$1,000 for each such violation. If such violation is a continuing one, each day of such violation shall constitute a separate offense: Provided, That this subsection shall not apply to members of the Armed Forces of the United States, or those civilian employees of the Department of Defense who are subject to the provisions of the Uniform Code of Military Justice, while engaged in the performance of their official duties; and the appropriate military authorities shall be responsible for taking any necessary disciplinary action with respect thereto and for making to the Administrator or Board, as appropriate, a timely report of any such action taken.

(2) Any such civil penalty may be compromised by the Administrator in the case of violations of titles III, V, VI, or XII, or any rule, regulation, or order issued thereunder, or by the Board, in the case of violations of titles IV or VII, or any rule, regulation, or order issued thereunder, or under section 1002(i), or any term, condition, or limitation of any permit or certificate issued under title IV, or by the Postmaster General in the case of regulations issued by him. The amount of such penalty, when finally determined, or the amount agreed upon in compromise, may be deducted from any sums owing by the United States to the person charged.

* * * * *

CRIMINAL PENALTIES

General

Sec. 902. [72 Stat. 784, as amended by 75 Stat. 466, 76 Stat. 150, 76 Stat. 921, 49 U.S.C. 1472] (a) Any person who knowingly and willfully violates any provision of this Act (except titles III, V, VI, VII, and XII), or any order, rule, or regulation issued by the Administrator or by the Board under any such provision or any term, condition, or limitation of any certificate or permit issued under title IV, for which no penalty is otherwise provided in this section or in section 904, shall be deemed guilty of a misdemeanor and upon conviction thereof shall be subject for the first offense to a fine of not more than \$500, and for any subsequent offense to a fine of not more than \$2,000. If such violation is a continuing one, each day of such violation shall constitute a separate offense.

* * * * *

TITLE X--PROCEDURE

* * * * *

JUDICIAL REVIEW OF ORDERS

Orders of Board and Administrator subject to Review

Sec. 1006. [72 Stat. 795, as amended by 74 Stat. 255, 75 Stat. 497, 49 U.S.C. 1486] (a) Any order, affirmative or negative, issued by the Board or Administrator under this Act, except any order in respect of any foreign air carrier subject to the approval of the President as provided in section 801 of this Act, shall be subject to review by the courts of appeals of the United States or the United States Court of Appeals for the District of Columbia upon petition, filed within sixty days after the entry of such order, by any person disclosing a substantial interest in such order. After the expiration of said sixty days a petition may be filed only by leave of court upon a showing of reasonable grounds for failure to file the petition theretofore.

Venue

(b) A petition under this section shall be filed in the court for the circuit wherein the petitioner resides or has his principal place of business or in the United States Court of Appeals for the District of Columbia.

Notice to Board or Administrator; Filing of Transcript

(c) A copy of the petition shall, upon filing, be forthwith transmitted to the Board or Administrator by the clerk of the court, and the Board or Administrator shall thereupon file in the court the record, if any, upon which the order complained of was entered, as provided in section 2112 of title 28, United States Code.

Power of Court

(d) Upon transmittal of the petition to the Board or Administrator, the court shall have exclusive jurisdiction to affirm, modify, or set aside the order complained of, in whole or in part, and if need be, to order further proceedings by the Board or Administrator. Upon good cause shown and after reasonable notice to the Board or Administrator, interlocutory relief may be granted by stay of the order or by such mandatory or other relief as may be appropriate.

Findings of Fact Conclusive

(e) The findings of facts by the Board or Administrator, if supported by substantial evidence, shall be conclusive. No objection to an order of the Board or Administrator shall be considered by the court unless such objection shall have been urged before the Board or Administrator or, if it was not so urged, unless there were reasonable grounds for failure to do so.

Certification or Certiorari

(f) The judgment and decree of the court affirming, modifying, or setting aside any such order of the Board or Administrator shall be subject only to review by the Supreme Court of the United States upon certification or certiorari as provided in section 1254 of title 28, United States Code.

* * * * *

Section 203(e) of the Revenue Act of 1964 (78 Stat. 35, 26 U.S.C.

38 note):

SEC. 203. REPEAL OF REQUIREMENT THAT BASIS OF SECTION 38 PROPERTY BE REDUCED BY 7 PERCENT; OTHER PROVISIONS RELATING TO INVESTMENT CREDIT.

* * * * *

(e) Treatment of Investment Credit by Federal Regulatory Agencies.-- It was the intent of the Congress in providing an investment credit under section 38 of the Internal Revenue Code of 1954, and it is the intent of the Congress in repealing the reduction in basis required by section 48(g) of such Code, to provide an incentive for modernization and growth of private industry (including that portion thereof which is regulated). Accordingly, Congress does not intend that any agency or instrumentality of the United States having jurisdiction with respect to a taxpayer shall, without the consent of the taxpayer, use--

(1) in the case of public utility property (as defined in section 46(c)(3)(B) of the Internal Revenue Code of 1954), more than a proportionate part (determined with reference to the average useful life of the property with respect to which the credit was allowed) of the credit against tax allowed for any taxable year by section 38 of such Code, or

(2) in the case of any other property, any credit against tax allowed by section 38 of such Code, to reduce such taxpayer's Federal income taxes for the purpose of establishing the cost of service of the taxpayer or to accomplish a similar result by any other method.

* * * * *

Relevant excerpts from the Administrative Procedure Act (60 Stat. 237, 5 U.S.C. 1001 et seq.):

JUDICIAL REVIEW

Sec. 10. [60 Stat. 243, 5 U.S.C. 1009] Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion--

(a) RIGHT OF REVIEW.--Any person suffering legal wrong because of any agency action, or adversely affected or aggrieved by such action within the meaning of any relevant statute, shall be entitled to judicial review thereof.

(b) FORM AND VENUE OF ACTION.--The form of proceeding for judicial review shall be any special statutory review proceeding relevant to the subject matter in any court specified by statute or, in the absence or inadequacy thereof, any applicable form of legal action (including actions for declaratory judgments or writs of prohibitory or mandatory injunction or habeas corpus) in any court of competent jurisdiction. Agency action shall be subject to judicial review in civil or criminal proceedings for judicial enforcement except to the extent that prior, adequate, and exclusive opportunity for such review is provided by law.

(c) REVIEWABLE ACTS.--Every agency action made reviewable by statute and every final agency action for which there is no other adequate remedy in any court shall be subject to judicial review. Any preliminary, procedural, or intermediate agency action or ruling not directly reviewable shall be subject to review upon the review of the final agency action. Except as otherwise expressly required by statute, agency action otherwise final shall be final for the purposes of this subsection whether or not there has been presented or determined any application for a declaratory order, for any form of reconsideration, or (unless the agency otherwise requires by rule and provides that the action meanwhile shall be inoperative) for an appeal to superior agency authority.

* * * * *

Section 322 of the Transportation Act of 1940 (54 Stat. 955,
49 U.S.C. 66):

(Prior to 1958 amendment)

Sec. 66. Government traffic; payment for transportation;
deduction of overpayments

Payment for transportation of the United States mail and of persons or property for or on behalf of the United States by any common carrier subject to the Interstate Commerce Act, as amended, or the Civil Aeronautics Act of 1938, shall be made upon presentation of bills therefor, prior to audit or settlement by the General Accounting Office, but the right is reserved to the United States Government to deduct the amount of any overpayment to any such carrier from any amount subsequently found to be due such carrier. Sept. 18, 1940, c. 722, Title III, Sec. 322, 54 Stat. 955.

(After 1958 amendment) 1/

Sec. 66. Government traffic; payment for transportation;
deduction of overcharges

Payment for transportation of the United States mail and of

1/ Sec. 3 of the amendatory act, Pub. L. 85-762, 72 Stat. 860, provides: "The provision of this Act which amends section 322 of the Transportation Act of 1940 [this section] shall apply only to transportation performed and payment made therefor subsequent to the effective date of this Act [August 26, 1958]."

persons or property for or on behalf of the United States by any common carrier subject to the Interstate Commerce Act, as amended, or the Civil Aeronautics Act of 1938, shall be made upon presentation of bills therefor, prior to audit or settlement by the General Accounting Office, but the right is reserved to the United States Government to deduct the amount of any overcharges by any such carrier from any amount subsequently found to be due such carrier. The term "overcharges" shall be deemed to mean charges for transportation services in excess of those applicable thereto under the tariffs lawfully on file with the Interstate Commerce Commission and the Civil Aeronautics Board and charges in excess of those applicable thereto under rates, fares, and charges established pursuant to section 22 of this title: Provided, however, That such deductions shall be made within three years (not including any time of war) from the time of payment of bills: Provided further, That every claim cognizable by the General Accounting Office for charges for transportation within the purview of this section shall be forever barred unless such claim shall be received in the General Accounting Office within three years (not including any time of war) from the date of (1) accrual of the cause of action thereon, or (2) payment of charges for the transportation involved, or (3) subsequent refund for overpayment of such charges, or (4) deduction made pursuant to this section, whichever is later. As amended Aug. 26, 1958, Pub. L. 85-762, Sec. 2, 72 Stat. 860.

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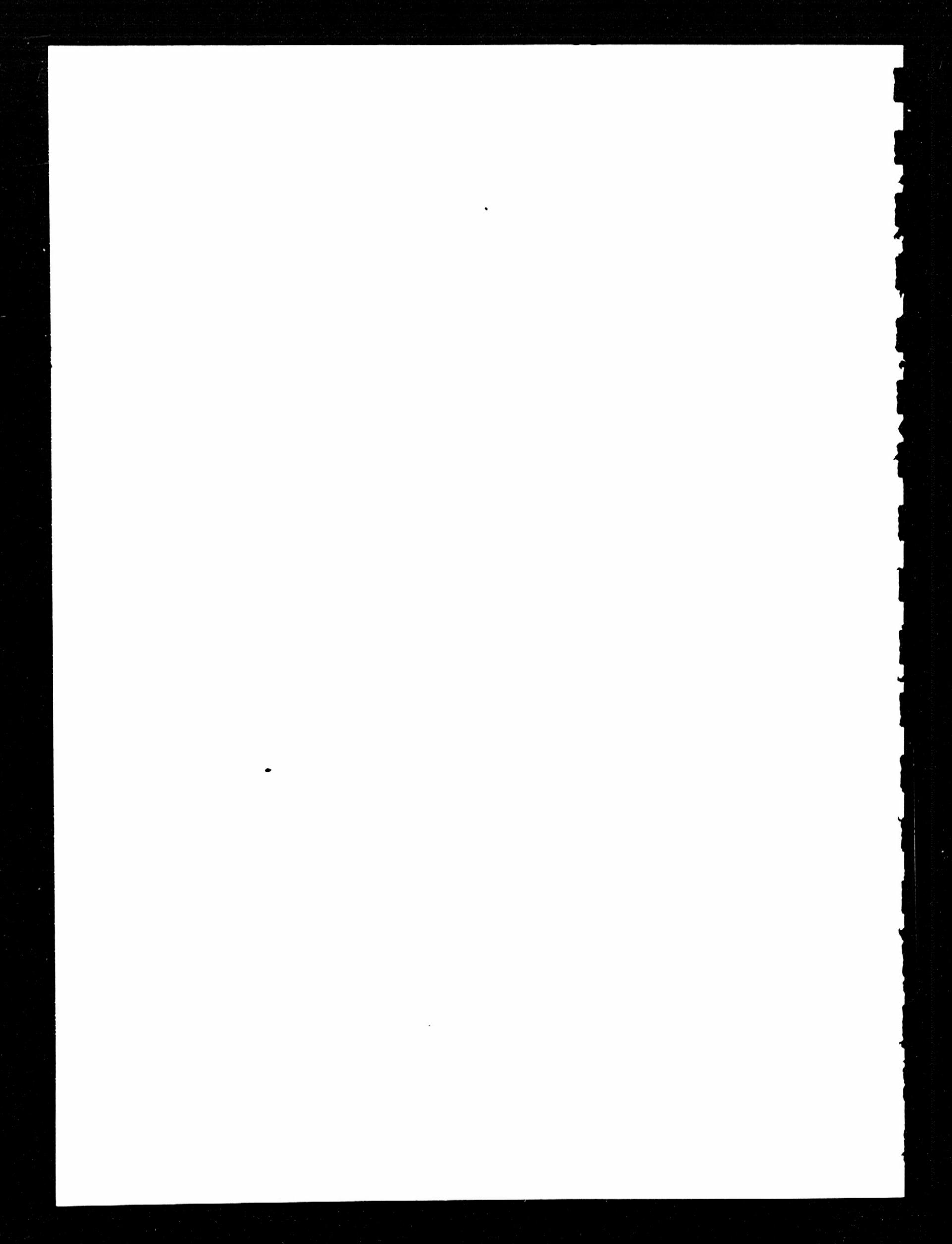
Relevant excerpts from the Judicial Code (62 Stat. 869, 28 U.S.C. 1 et seq.):

CHAPTER 91--COURT OF CLAIMS

Sec. 1491. Claims against United States generally

The Court of Claims shall have jurisdiction to render judgment upon any claim against the United States:

- (1) Founded upon the Constitution; or
- (2) Founded upon any Act of Congress; or
- (3) Founded upon any regulation of an executive department; or
- (4) Founded upon any express or implied contract with the United States; or
- (5) For liquidated or unliquidated damages in cases not sounding in tort. June 25, 1948, c. 646, 62 Stat. 940.



APPENDIX B

Excerpts from Order E-21277, August 28, 1964

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h. Income taxes - The profit-sharing provisions of Class Rate III relating to income tax are based on the Board's "actual tax" policy which was first established in the 1951 Western-Inland Case,^{16/} and which has been applied unswervingly by the Board since that time in both individual subsidy rate cases and the prior class rates. The application of this principle will be the same under the new class rate as it was under the prior class rates. However, for purposes of clarity and to resolve certain areas of misunderstanding which have arisen under Class Rate II, some language changes have been made. Generally, the trouble areas, each of which will be discussed in turn, involve (1) investment tax credit, (2) the treatment given taxes related to income which is not otherwise considered in the profit-sharing determination for a given year, and (3) the treatment to be given amendments or revisions in tax returns for prior class rate years which are made after the profit-sharing determinations for those years have been made. .

Investment tax credit - Class Rate III provides that taxes shall be determined on the basis of the carrier's actual income taxes as reported on its income tax returns, including the reduction of taxes resulting from investment tax credits derived under section 38 of the Internal Revenue Code of 1954, as amended. The specific reference to investment tax credits in no way changes the actual tax provisions as set forth in Class Rates I and II, but is intended merely to make clear our position with respect to the treatment of such credits in the light of the provisions of section 203(e) of the Revenue Act of 1964 (78 Stat. 19).

The actual tax policy is intended to insure that the Board, in determining the amount of subsidy to which a carrier is entitled, will provide an allowance for taxes which is no greater than the taxes actually paid by the carrier. Hence, in the Western-Inland Case, supra, the Board rejected the notion that the tax element should cover constructed taxes which the carrier would have paid if it had not incurred the expenses which were being disallowed for subsidy purposes. By the same token, the Board has refused to provide, in a past period subsidy case, an allowance for taxes which were deferred

^{16/} Western Air Lines, Inc. and Inland Air Lines, Inc., Mail Rates, 14 C.A.B. 243, 251-255 (1951).

under the liberalized depreciation provisions of section 167 of the Internal Revenue Code of 1954, as amended, on the ground that only actual taxes are recognizable.^{17/} In fact, in two individual subsidy cases ^{18/} and in one profit-sharing case,^{19/} the Board has considered the reduction of taxes resulting from investment tax credits in making its final determinations.

On its face, the language of section 203(e) of the Revenue Act of 1964 ^{20/} may raise some questions as to the application of the actual tax policy with respect to taxes saved by the carrier through investment tax credits. At first glance, the section might appear to encompass all rate-making by federal regulatory agencies (although there is doubt as to whether fixing subsidy rates for developmental purposes is "establishing the cost of service" of an air carrier), and, thus, to

^{17/} Reopened Pan American Mail Rate Case, (Order to Show Cause) E-18018, p. 34, February 13, 1962, (Final Order) E-18072, March 5, 1962. This case distinguished the rule applied in subsidy cases from the rule applied in commercial rate cases.

^{18/} Alaska Coastal-Ellis Airlines, Mail Rates, (Provisional Statement) E-20790, May 5, 1964, (Final Order) E-20835, May 19, 1964; Aloha Airlines, Subsidy Mail Rates, (Provisional Statement) E-21138, (Final Order) E-21179, August 11, 1964.

^{19/} Bonanza Air Lines, Inc., 1962 Subsidy Refund, Order E-21137, July 30, 1964.

^{20/} Section 203(e) provides:

"It was the intent of the Congress in providing an investment credit under section 38 of the Internal Revenue Code of 1954 . . . to provide an incentive for modernization and growth of private industry (including that portion thereof which is regulated). Accordingly, Congress does not intend that any agency or instrumentality of the United States having jurisdiction with respect to a taxpayer shall, without the consent of the taxpayer, use [such credit allowed under section 38 of the code] to reduce such taxpayer's Federal income taxes for the purpose of establishing the cost of service of the taxpayer or to accomplish a similar result by any other method."

preclude the application of the actual tax policy to investment tax credits even in subsidy cases. However, there is nothing in the legislative history of the Revenue Act which indicates that Congress even considered the consequences of section 203(e) in subsidy rate-making proceedings. To the contrary, the legislative history is clear that the purpose of the provision is to prevent a flow-through to "consumers" (the "customer of the utility") of the benefits of the credit, so that the utility can enjoy the incentives for improvement and expansion which the credit provides.^{21/} While there were isolated references in the legislative history to air carriers and the Board, they related to the flow-through concept,^{22/} and did not broach subsidy questions. To infer that a statute materially alters a fundamental principle of subsidy rate regulation (the actual tax policy in this case), it must clearly appear that Congress intended such an effect.^{23/} There is no such clear indication in section 203(e) or its legislative history.

21/ The report of the House Ways and Means Committee (H. Rept. No. 749, September 13, 1963, accompanying H.R. 8363) states clearly that ". . . [i]n the case of the investment credit the bill . . . prevents regulatory commissions in certain cases from requiring the 'flow through' of the benefits of the investment credit to the customers of regulated industries . . ." The same statement was made in Senate Report No. 830, January 28, 1964, and statements in the debate were to the same effect. E.g., 110 Cong. Rec. 1231 and 1439.

22/ Typical of such comments was one by Senator Long who said:

"So far as the CAB is concerned, that regulatory agency does not fix the rates of the airline. Those rates are fixed by competition. Therefore, so far as that agency is concerned, this does not make any difference."

"So there is no real reason why that agency should become involved one way or the other . . ."

Obviously, the Senator was talking about the filing with the Board of commercial rate tariffs which automatically become effective within a specified time if not suspended by the Board.

23/ See Panhandle Eastern Pipe Line Company v. Federal Power Commission, 316 F. 2d 659 (D.C. Cir., 1963), cert. den. 375 U.S. 881 (1963).

Actually, the results intended by section 203(e) for other regulated industries and nonsubsidized airlines - that is, the encouragement of development and expansion - are already provided for subsidized airlines by section 406(b) of the Federal Aviation Act, which controls the establishment of the class rate. Section 406(b) requires the Board in fixing subsidy rates to take into consideration:

" . . . the need of each such air carrier . . . for compensation . . . sufficient . . . to enable such air carrier . . . to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

In other words, Congress has provided a comprehensive scheme for fulfilling the need of air carriers for resources to maintain and continue the development of air transportation. If need has been otherwise met under this provision, which was designed to meet the special problems of the airline industry (particularly the subsidized airlines) for certain purposes, it can hardly be argued that the carriers "need" the benefit of the investment tax credit for the same purposes. The adoption of such a position would merely serve to provide the carriers with subsidy in excess of need, - that is, additional subsidy to cover taxes they do not pay - thereby contravening the provisions of section 406. In accordance with established canons of statutory construction, we prefer to read section 203(e) and section 406 as compatible, not contradictory. However, if there is a conflict between the two, it would seem that the Federal Aviation Act would control since it is the "special" or "dominant" statute which was designed to insure the maintenance and continued development of air transportation in the interest of the commerce of the United States, the Postal Service, and the national defense.

The carriers have indicated informally that they oppose the treatment of the investment tax credit stated above. If they wish to pursue this opposition, the Act and the Board's Rules of Practice afford them adequate opportunity to have any objections to this rate, including those related to the investment tax credit, considered in a formal proceeding, and, if they are not thereafter satisfied with the Board's disposition of these matters, to petition for judicial review. However, the carriers seek a departure from the traditional method of challenging rates proposed by the Board. They request that language be included in Class Rate III which would preserve for each carrier the right to challenge the tax provision in the courts at a later date, either in a special investment tax credit proceeding or after the provision is applied to the carrier in a future profit-sharing determination under Class Rate III. We are of the opinion that granting the carriers' request would not be consistent with the Board's Rules of Practice nor with the concept of finality of rates. Accordingly, the request is denied.

